VII. Bilateral Negotiations

Asia and the Pacific

The past year and a half has been a period of significant financial and economic difficulties in many Asia-Pacific countries. The financial crisis began in mid-1997 with the depreciation of the Thai baht, thereafter spreading to other countries. The ensuing, adverse economic circumstances experienced in the Asia-Pacific region have contrasted sharply with its previous decades of some of the world's fastest economic growth. Several Asian economies -- Korea, Thailand, Indonesia and Malaysia -- have contracted by 6% or more. Many others are in recession or close to it. Asian currencies may have stabilized, but relative economic and social conditions have deteriorated.

This period of financial crisis represents both a challenge and opportunity for these countries and for U.S. trade and investment policy. The Asian financial crisis has affected U.S. trade significantly, primarily in the form of reduced demand for U.S. exports in the affected economies, but also in the guise of increased U.S. imports in sensitive industrial areas. With increased pressures on import-sensitive industries, U.S. producers and workers are experiencing lost manufacturing jobs, declining farm incomes, and suffered a loss of $30 billion in exports to the Pacific Rim last year. And while the solution ultimately lies with the people, governments and private sectors of the affected countries, the United States remains committed to open market principles, and rejects any broad protectionist response to the crisis. With exports to Asia off $30 billion and a goods trade deficit at $250 billion in 1998 and perhaps $300 billion this year, this requires some sacrifice. The United States has nonetheless kept its market open while enforcing its laws on dumping and import surges, and urged Japan, Europe and others to share the burden. The greatest contribution the United States and other industrial countries can make is to offer healthy and open markets for fairly traded exports.

There is acknowledgment today that the financial crisis resulted, in part, from excessively close ties between government, banks, and corporations that fostered unsound lending practices, interventionist industrial policies and a lack of market-based disciplines -- all sheltered by a non-transparent, and virtually non-existent, regulation of financial markets. These close ties also led to structural impediments in the form of monopolies, trade restrictive practices, and border and internal market barriers. Some of the countries affected by the financial crisis have begun a return to sustained, healthy economic growth by moving to adopt the type of trade policy changes that the United States has consistently advocated: enhanced market access, transparency, economic deregulation and investment decisions based upon market disciplines.

U.S. trade policy objectives complement firmly the goals of financial market stabilization, as evidenced by the strong emphasis on structural reform in the International Financial Institution (IFI)s' programs. The United States will continue to support these reform and stabilization packages, with the IMF at the center and augmented by the $10 billion program the USG and Japan announced last November. These packages are now showing their value. As Thailand and Korea, in particular, have implemented their reforms, their currencies have regained stability; a growing transparency and market openness has begun to raise investor confidence; and one may observe the initial signs of a return to economic health.

Despite the change in economic landscape in 1998, Asia-Pacific remains a vital trade region. U.S. total trade (i.e. imports and exports) across the Pacific is estimated to be 72 percent greater than across the Atlantic; merchandise exports to Asia have grown over 52 percent since 1990. In 1998, APEC members received over 60 percent of U.S. merchandise exports and accounted for more than two-thirds of our imports.

Trade and investment interaction between the United States and Asia will continue to be both rewarding and challenging in 1999. The re-emergence of growth in some Asian economies should promote renewed purchases of U.S. agricultural commodities and industrial products, as well as demand for U.S. investment. The United States also will continue to press bilaterally, regionally, and multilaterally in the WTO and APEC for greater market access for U.S. exports of goods, services, and investment. The ongoing work of the WTO, the work of this year's Ministerial, and the efforts of the IFIs' offer continuing opportunities to open further Asian markets. Reducing many of these barriers to the expansion of U.S.-Asian trade will benefit both economic regions for decades to come. The United States will continue to seek full and effective implementation of the results of the Uruguay Round, in addition to full compliance with all WTO provisions, including bringing cases of alleged WTO inconsistency to the Dispute Settlement Body for adjudication. Trade barriers remain prevalent in many sectors in the Asia-Pacific region and strong enforcement work may be anticipated in the interest of ensuring that multilateral and bilateral trading rights and obligations are honored.

Australia and New Zealand

This past year saw the opening of New Zealand's market to U.S. salmon exports. The WTO has decided that Australia should bring its sanitary and phytosanitary regime into compliance with the WTO SPS Agreement. At this writing, the implementation of the WTO Dispute Settlement Body's decision is in process. The United States also is in the midst of WTO dispute settlement with Australia with regard to its export subsidies of automotive leather. The final report of the dispute settlement panel is due in late March.

Republic of Korea

Macroeconomic Stabilization and Trade

At the end of 1997, the IMF negotiated a macroeconomic stabilization package with the Korean Government when the value of the *won* depreciated dramatically due to a large outflow of foreign investment. The stabilization package for Korea included credit from the IMF, the World Bank, the Asian Development Bank, and several countries that agreed to bilateral contributions as a "second line of defense."

The stabilization plan focused on (1) restructuring the financial and corporate sectors to make them more sound, efficient, transparent, and open to foreign investment; and (2) eliminating trade-and competition-distorting policies through structural reforms. These structural changes include (1) early elimination of WTO-prohibited export and domestic content subsidies and the import diversification program (which prohibits Japanese imports); and (2) a reduction in the number of products subject to tariff adjustments, or snapbacks. Korea also agreed to liberalize its import licensing and certification procedures and to bind its OECD financial services market access commitments in the WTO.

The Korean Government's record on implementation of some of its trade-related stabilization commitments has "fallen short of the mark." Specifically, Korea has not implemented its commitment to bind in the WTO its OECD market access commitments on financial services. In addition, the U.S. Government has expressed concern about the Korean Government's decision to maintain tariffs at the highest "snapback" level, while eliminating the "snapback," or tariff adjustment mechanism. The U.S. Government will continue to work with Korea to ensure full follow-through on its trade-related stabilization commitments.

The Korean Government has made substantial progress on some of its stabilization commitments throughout 1998, particularly in the financial sector through rationalizing, recapitalizing, and easing interest rates. Regulations have been adopted to accelerate corporate restructuring. For example, international standards on accounting and the corporate decision-making processes have been implemented. The rights of small shareholders have been strengthened, while restrictions on foreign participation have been eased. Cross payment guarantees among major corporations are being eliminated, and bankruptcy laws have been amended. The latter have facilitated the collapse of uncompetitive companies.

While ties between the government, banks, and the corporate conglomerates have been weakened, the "Big Deals" (the restructuring of conglomerates through mergers and business swaps to reduce over-capacity and improve efficiency) have not progressed smoothly. There is concern that the restructuring deals will be done in an anti-competitive way, and that government-controlled banks are extending financial favors to chaebols in exchange for undergoing these necessary but painful reforms.

The sound fiscal, monetary, and restructuring policies adopted by the Kim Dae Jung administration have contributed toward a resumption of foreign and domestic/consumer confidence in Korea's economy. Several macroeconomic forecasters, including the IMF, are predicting a return to positive growth in 1999, while Korea's sovereign ratings have been upgraded to investment status for the first time since the foreign crisis began. Corporate investment, domestic consumption, and imports are expected to resume growth in 1999; however, Korea is still expected to run both global and U.S. bilateral trade surpluses again.

OECD

In late 1996, the Korean National Assembly ratified Korea's accession to the OECD. In May 1997, on the fringes of an OECD Ministerial, Korea issued a statement indicating that the government did not support anti-import activities, which had been encountered in the Korean market in the context of the frugality, or anti-consumption, campaign launched by President Kim Young-Sam. The Korean also promulgated guidelines to trade officials to ensure that they did not discriminate against imports. The U.S. continues to closely monitor U.S.-Korea trade to guard against systemic anti-import behavior, such as in the motor vehicle sector.

In the fall of 1997, the Trade Committee of the OECD reviewed the terms of Korea's accession. In this review, the U.S. flagged its concerns about Korea's trade regime -- specifically, its market-access and distribution restrictions on autos, telecommunications, cosmetics, and pharmaceuticals, as well as Korea's lengthy and burdensome import clearance procedures. The United States also noted its expectation that Korea would implement its WTO commitments as a *developed* economy, and in addition, negotiate *future* agreements, including on agriculture, as such.

Korea has not implemented its stabilization-related commitment to bind its OECD financial services market access commitments in the WTO. The U.S. Government will continue to work with the Republic of Korea to ensure that it fulfills this commitment.

Auto Market Access (Super/Section 301)

In the October 1, 1997 Super 301 report to the Congress, the USTR identified Korean barriers to motor vehicles as a priority foreign country practice. Specific Korean practices of concern that were cited included an array of cumulative tariff and tax disincentives disproportionately affecting imports, onerous and costly auto standards and certification procedures, auto financing restrictions, and a cumulative climate of bias against imported vehicles. On October 20, 1997, the USTR initiated a Section 301 investigation with respect to certain acts, policies and practices of the Government of the Republic of Korea that pose barriers to imports of U.S. autos into the Korean market.

After intense bilateral negotiations, on October 20, 1998, the U.S. and Korea concluded a Memorandum of Understanding (MOU) to improve market access for foreign motor vehicles. Under this MOU, Korea agreed to (1) bind in the WTO its 80% applied tariff rate at 8%; (2) lower some of its motor-vehicle-related taxes and to eliminate others; (3) adopt a self-certification system by 2002; (4) streamline its standards and certification procedures; (5) establish a new financing mechanism to make it easier to purchase motor vehicles in Korea; and (6) continue to actively and expeditiously address instances of anti-import activity.

Following the negotiation of this MOU, the USTR determined that certain acts, policies and practices of the Government of Korea related to exports of U.S. motor vehicles are unreasonable and discriminatory and burden or restrict U.S. commerce, but recognized that the Korean Government had agreed to take several measures to resolve the matters under investigation. Thus, the USTR decided on October 20, 1998, to terminate the investigation and to monitor the Korean Government's implementation of these measures to eliminate those trade practices. The first formal review of Korea's implementation of the 1998 MOU will take place no later than April 30, 1999.

Intellectual Property Protection

In April 1997, the U.S. downgraded Korea from the Special 301 "*priority* watch list" to the "watch list" after Korea agreed to an action plan on specific reforms. Korea has subsequently made significant efforts to strengthen its Intellectual Property Rights (IPR) laws and enforcement. Korea maintained its "watch list" status in 1998, although there have been inconsistencies with respect to court interpretations and rulings on the law. A revised trademark law became effective and a new patent court was established on March 1, 1998. The Korean has concentrated on prosecution (3 percent more infringement cases were reported and 32 percent more individuals were arrested in 1998), strengthened penalties, and sponsored public awareness seminars. U.S. industry, however, remains concerned about restrictions on patent term extension for certain pharmaceutical, cosmetic, agrochemical, and animal health products that are subject to lengthy clinical trials and domestic testing requirements.

Although a law permitting patent extension was adopted on January 1, 1999, Korea has still failed to provide full protection to pre-existing copyrighted works as required under TRIPS. This failure precludes the protection of some famous cartoon characters and textile designs.

The Korean Government has amended the Unfair Competition Protection Act by increasing the penalties for leaking trade secrets and propriety information or data from foreign firms. That said, the U.S. pharmaceutical industry has continued to experience data protection problems. In fact, the protection of proprietary test data submitted by pharmaceutical companies against "unfair commercial use" by competitors has been weakened by recent regulations.

The U.S. Government will continue to work with the Korean Government to ensure its full compliance with its TRIPS Agreement obligations, including those on protection of test data against unfair commercial use and retroactive protection of copyrights. The U.S. Government has urged Korea to improve coordination between its health and safety and IPR officials to ensure that products that infringe existing patents are not approved for marketing. The U.S. Government has indicated to the Korean Government that issues related to Korea's TRIPS consistency must be resolved before signature of a Bilateral Investment Treaty (BIT). Also, Korea's overall record on providing IPR protection -- *e.g.,* for patents -- and its Special 301 status constitute important indicators of the nature Korea's business climate.

Pharmaceuticals

For well over a year, the U.S. Government and pharmaceuticals industry have been discussing with the Korean Government a number of concerns about treatment of, and market access for, foreign research-based pharmaceuticals in Korea. The primary U.S. concerns relate to three baskets of issues: (1) listing and pricing on Korea's national health insurance reimbursement schedule, and associated hospital margins and administrative procedures on dispensing; (2) protection of intellectual property rights (IPR), particularly protection of clinical data and patents; and (3) regulatory requirements, particularly for clinical testing. The Korean Government has taken some steps to address U.S. concerns – *e.g.*, by committing to list imported pharmaceuticals on Korea's national health insurance reimbursement schedule by no later than July 1, 1999, and by eliminating the requirement for the submission of a Certificate of Free Sale before Phase III clinical trials can commence in Korea. That said, to comprehensively and definitively address U.S. concerns, the Korean Government must advance progress further. The U.S. Government will continue to press the Korean Government on pharmaceuticals trade issues until U.S. concerns are fully and satisfactorily addressed.

Telecommunications (Section 1377 Review and Section 1374 Identification)

In 1989, Korea was first identified as a "priority foreign country" (PFC) under Section 1374 of the Omnibus Trade and Competitiveness Act of 1988 (OTCA). Problems cited at that time included discriminatory procurement practices, "buy local" policies, lack of transparency, and inadequate trade secret protection. In February 1992, USTR negotiated a comprehensive agreement covering value-added services, standards, procurement, and equipment authorization. In 1993, the United States and Korea exchanged letters regarding the implementation of the 1992 agreement. In 1995, Korean discriminatory practices again were identified by a number of companies during the Section 1377 review. In an exchange of letters, Korea agreed to resolve several company-specific problems; for instance, one major telecommunications company was allowed to bid in the 1995 procurement cycle. This procurement was postponed until early 1996.

In the context of the 1996 Section 1377 review, the United States and Korea reached an understanding on outstanding problems concerning implementation of the 1990 and 1992 bilateral telecommunications trade agreements. The 1996 agreement elaborates on aspects of the existing agreements and commits Korea to several reforms, specifically (1) equal treatment in procurement of advanced technologies; and (2) effective protection of U.S. intellectual property rights. In 1996, the Korean also committed to starting talks to address U.S. telecommunications concerns outside of the scope of the existing agreements. These talks were conducted in parallel with USTR's review of existing agreements to determine whether they adequately achieved the market access objectives specified in the 1988 Telecommunications Trade Act. As a result of this review, on July 26, 1996, USTR identified Korea as a PFC under Section 1374 of the OTCA.

The Administration has subsequently engaged in consultations with Korea and achieved some progress toward the settlement of outstanding issues. In June 1997, the U.S. and Korean Governments concluded the negotiation of a Korean policy statement that addressed remaining U.S. concerns. On July 23, 1997, USTR Barshefsky announced her intention to revoke the PFC designation after allowing a period for public comment. The revocation became effective August 11, 1997.

The current Korean administration's efforts to expand foreign investment in telecommunications companies have encountered resistance from the National Assembly. The Korean Government, however, plans to resubmit its proposal to raise the ceiling on foreign ownership from 33 to 49 percent, and believes the Assembly will approve it this year. Also, U.S. industry has recently become concerned about press reports indicating that the Korean Government is pressuring private cellular telecom operators and wire-line companies to consolidate under the Big Deal programs. The Korean Government has indicated that it is not its policy to urge such consolidations. The U.S. Government will closely monitor the situation.

Steel

On June 1, 1995, the Committee on Pipe and Tube Imports (CPTI) filed a Section 301 petition alleging that Korea (1) restricts exports of domestically-produced steel sheet; (2) controls domestic prices below world prices; and (3) restricts exports of pipe and tube products to the EU and instead, diverts these exports to the U.S. market. On July 11, 1995, the CPTI agreed to withdraw its petition in light of Korea's agreement to establish a consultative mechanism for one year to increase transparency *vis-a-vis* production and trade of Korea's steel-sheet and pipe and tube products. Korea also agreed to (1) notify the United States of any measure to control steel production, pricing, or exports; and (2) ensure that the government was no longer interfering with pricing or production. In July 1996, the one-year agreement was extended for another year. Korea has regularly provided data required by the agreement, and bilateral consultations were held in May and November 1996, and in 1997. In these meetings, the United States raised its ongoing concern that the Korean Government is influencing private-sector decisions concerning steel. Also in 1997, at the request of U.S. industry, the U.S. Government asked, and Korea responded to, specific questions on the operation of Hanbo Steel.

U.S. steel imports surged in 1998, as chronic overcapacity in the steel sector was compounded by the Asian financial crisis and a corresponding drop in demand in Asia. Public and Congressional pressure on the Clinton Administration to provide relief has been intense. Korea accounted for nearly 20 percent of the overall growth in U.S. imports of steel in 1998.

In June and November of 1998, President Clinton stressed to Korean President Kim Dae Jung the need for the Korean Government to address U.S. concerns about steel. In August, the U.S. and Korean Governments concluded an exchange of letters in which the Korean Government provided assurances that it will not support Hanbo and that the impending sale of the company will be managed by an independent international agent and market-driven. In July of 1998, Hanbo's hot-rolled plant was shut down.

Following high-level exchanges on steel issues, the U.S. Government launched a comprehensive, intensive series of consultations to address U.S. steel concerns including about Hanbo, but going beyond the issues associated with this company. In these steel discussions, our aim is to ensure that real and substantive progress is made toward permanently getting the Korean Government out of the steel business. Specifically, we are pressing for the following:

(a) having the Korean Government address anticompetitive activity in the Korean steel sector and ensure open competition inside Korea and in international trade;

(b) expeditious, complete, and market-based privatization of Korea's largest steel producer, POSCO ;

(c) implementation of the Hanbo sale and operation of the company on arms-length terms as outlined in our August exchange of letters with Korea, in a manner which will not engender government involvement; and

(d) fair trade in steel products.

The U.S. Government has made clear that it will strongly enforce U.S. laws against unfair trade practices in steel through expedited investigations and other appropriate actions, and through the implementation of an early warning system to monitor import trends.

Beef

After a 1989 GATT panel ruling against Korea's measures on beef, Korea agreed to phase out its balance-of-payment restrictions on beef. Subsequently, in 1990, and in July of 1993, the United States and Korea concluded an exchange of letters under which Korea agreed to annual, increasing minimum market access levels for beef imports through 1995. The 1993 agreement also guaranteed direct commercial relations between foreign suppliers and Korean retailers and distributors and provided that a growing volume of beef be sold through that channel instead of through a quasi-governmental agency. Specifically, the agreement provided for (1) an increase in the minimum annual quotas; (2) an increase in the number of Korean meat outlets and retailers that can undertake commercial transactions with U.S. exporters without Korean Government intervention -- the Simultaneous Buy/Sell (SBS) system; (3) dramatically increased annual SBS sub-quota amounts; and (4) a ceiling on the mark-up levied on the duty-paid price of imported beef. Australia and New Zealand -- the other two major suppliers of beef to Korea -- also entered into identical agreements on beef issues with Korea.

In December 1993, the provisions of the July agreement, including the increasing, annual minimum market access provisions, were extended after the United States, during the Uruguay Round, agreed to Korea's request to extend the phase-out period for balance-of-payment restrictions on beef to December 31, 2000. In short, the United States agreed to allow Korea to maintain its quantitative restrictions on beef imports after a GATT panel ruled that Korea had no legal right to maintain such restrictions, and in return, the United States was guaranteed increasing access to Korea's beef market through minimum quotas that expanded over time.

Pursuant to section 306 of the Trade Act, the USTR is monitoring Korea's implementation of its commitments on beef imports. The U.S. and Korean Governments have met quarterly on the specifics of Korea's implementation record on the 1993 agreements. In 1997, Korea did not meet its annual commitment to import 167,000 metric tons of beef. In 1998, Korea fell short of its 187,000 metric ton quota by as much as 60-80%.

Senior U.S. Government officials have repeatedly raised the beef issue in an attempt to establish a market-driven beef import system in Korea by eliminating government impediments to the entry and distribution of foreign beef. In September and November of 1998, the U.S. and Korean Governments held two rounds of talks, and in January 1999, sat down again in Washington to try to reach agreement on such a plan. As no agreement was reached over the course of these talks, the U.S. Government requested WTO dispute settlement consultations on February 1. Consultations will take place in March in Europe.

Cosmetics (Impediments to Entry and Distribution)

Impediments to entry and distribution of foreign cosmetic products in Korea include (1) Korean Food and Drug Administration (KFDA) approval required for imports of the same cosmetic products, if they have different countries of origin; (2) the Korean Government's delegation of authority to the domestic industry association to screen advertising and information brochures prior to use; (3) provision of proprietary information on imports to Korean competitors; (4) redundant testing; and (5) burdensome import authorization and tracking requirements. In July 1997, the Cosmetic, Toiletry, and Fragrance Association (CTFA) submitted a petition to the U.S. Government requesting that Korean trade practices affecting cosmetics be included in the Super 301 report.

During July and August 1997, U.S. Government officials made representations to Korean Embassy officials on the barriers cited by the industry. In September, Korean officials provided USTR with a written response to the industry submission to the Section 301 Committee indicating their intention to make some changes to address U.S. concerns. Nonetheless, the U.S. Government cited Korea's cosmetics-related measures as a bilateral priority in the 1997 Super 301 report, because the Korean Government still had not fully addressed U.S. concerns.

On January 1, 1998, the KFDA abolished the annual testing requirement for imported cosmetics and authorized importers to perform the required self-testing. Significant delays still remain for final approval from the Ministry of Health and Welfare (MHW) for the local sale of products developed outside of Korea. The U.S. Government will continue to press Korea in a variety of fora to address concerns on its barriers to entry and distrubution of cosmetics.

Financial Services

As a condition in the IMF stabilization package, Korea agreed to bind its OECD commitments on financial-services market access in the WTO. In April 1998, Korea liberalized insurance appraisals and activities ancillary to the management of insurance and pension funds. At the same time, the brokerage market was opened to foreign firms, and several reinsurance firms have since entered the market.

Distilled Spirits (WTO Dispute Settlement)

In 1996, the United States exported $1.4 million of whiskey to Korea, including $1.03 million of bourbon whiskey. Despite Korean consumer interest in U.S. whiskey, U.S. exports remain at very low levels and account for less than 1 percent of the total Korean market for distilled spirits because of the exorbitant taxes and tariffs they face. U.S. exports to Korea of other distilled spirits (rum, brandy, gin, vodka, cordials and liqueurs) totaled $443,000 in 1996. Korea's taxation of alcoholic beverages is based on a two-tiered taxation regime. First, under a general liquor tax law, Korea imposes an ad valorem tax of 100 percent on whiskey and brandy and of 80 percent on vodka, rum and gin. Meanwhile, Korea applies a tax of only 35% to Soju, its locally produced distilled spirit which has been compared to vodka. This differentiation is made even more dramatic by the application of an Education Tax that is higher when the liquor tax rates are higher. The result of this tax rate differentiation is a tax burden on U.S. whiskey that is over four times greater than the burden on Soju, assuming the actual prices were the same.

On January 18, 1999, the Appellate Body of the WTO affirmed the mid-1998 report of a dispute settlement panel that Korean taxes on distilled spirits violate WTO rules against discriminatory taxes. The case was brought before the WTO in late 1997 by the United States and the European Union. The Appellate Body report supports the U.S. challenge to two Korean laws that apply higher taxes to U.S. distilled spirits exports than to Korea's domestically produced distilled spirit, Soju. In its decision the panel found, and the Appellate Body agreed, that these taxes violate article III:2 of the General Agreement on Tariffs and Trade (GATT) because they afford protection to domestic production of Soju, an alcoholic beverage produced in Korea. In affirming the panel's ruling, the Appellate Body stressed that the GATT protects the maintenance of equality of competitive conditions for imported and domestic products. This case represents the first time a WTO Panel and the WTO Appellate Body have found against Korean measures.

Import Clearance Procedures

Korea maintains significant sanitary and phytosanitary (SPS) barriers that delay U.S. agricultural and food exports from entry into Korea, frequently for two to four weeks, but often for up to two months (except for perishable products, which take a maximum of five days). Problems in Korean import clearance procedures have arisen in the following areas: (1) sampling for inspection and testing; (2) fumigation for insects; (3) incubation testing for insects, including of horticultural products from certified "pest-free" areas; (4) sorting for separation of spoiled produce; (5) non-science-based standards and conformity assessment procedures in the Korean Food and Food Additives Codes; and (6) requirements for proprietary information on manufacturing process and ingredients (listing of *all, by percentage*).

The United States has been raising concerns about Korea's import clearance procedures for several years and initiated WTO dispute settlement consultations in April 1995. A number of consultations have been held in that context -- the most recent in January 1997 -- resulting in certain changes in Korean procedures. These include the (1) establishment of expedited (5 days) clearance procedures for fresh fruits and vegetables; (2) development of a new sampling system to replace 100 percent sampling; (3) abolition of sorting requirements for horticultural products; (4) elimination of mandatory incubation testing for California fruit; (5) using the concept of scientific risk assessment, development of a quarantine pest list to determine fumigation requirements; and (6) revision of some of the Korean food additives standards to bring them into closer conformity with *CODEX Alimentarious* standards. At the January 1997 consultations, Korean Government officials also stated that manufacturing process information and ingredient listing by percentage for *all* ingredients were no longer required for import clearance.

Following the January 1997 consultations, U.S. industry reported problems in Korean port inspectors' follow-through on import clearance changes, in particular, those related to proprietary information. In addition, some of the changes Korean officials were implementing did not adequately address U.S. concerns. The U.S. Government therefore raised the import clearance issue at several meetings of the WTO SPS Committee. Korean import clearance procedures also were cited as a bilateral priority in the 1997 Super 301 report. In October 1997, in bilateral consultations, and in the OECD's review of Korea's accession, USTR officials emphasized Korea's need to faithfully implement the changes to which it had committed in January.

The economic crisis spurred deregulation and a better trading environment seems to be developing. At the beginning of 1998, Korea announced its intention to bring its food code standards more into conformity with CODEX standards, reducing some entry problems for restrictive standards. Korea also revised its microorganism standards for meat and agricultural chemical standards for fresh fruit to bring them into conformity with international standards. The U.S. Government will continue to pursue liberalization of Korean import procedures until clearance times and procedures in Korean ports of entry are based on science and consistent with international norms and, in the case of procedures, based on science. Methods include action in the WTO, OECD, and bilateral consultations, as well as through the implementation of related conditions in the IMF stabilization package for Korea.

1995 Shelf-Life Agreement (Implementation)

In November 1994, USTR accepted a Section 301 petition filed by the National Pork Producers' Council, the American Meat Institute, and the National Cattlemen's Association, alleging that a number of Korean practices -- especially government-mandated shelf-life limits and long delays at the port -- have effectively prohibited U.S. meat imports. As a result of WTO dispute settlement consultations with the United States, in July 1995, Korea agreed to phase out its government-mandated shelf-life requirements on certain products and to allow manufacturers to set their own "sell-by" dates. Korea agreed to implement the manufacturer-determined shelf-life system by October 1, 1995, for shelf-stable dried, packaged, canned or bottled products, and by July 1, 1996, for chilled, vacuum-packed meat and frozen food. The 1995 Agreement also covered other concerns raised in the petition, such as pork tendering procedures and temperature requirements.

In June 1998, Korea abolished government-mandated shelf-life requirements for 66 food items, including sterilized milk products. Shelf-life requirements remain on 21 food items, mainly products that deteriorate quickly. The KFDA also initiated a project to bring Korea's food codes and labeling standards in conformance with international standards by the end of 1999. The U.S. Government will continue to work with the Korean Government to ensure that the 1995 Shelf-life Agreement is implemented fully and faithfully.

Screen Quotas

Korean Law requires that domestic films be shown in each cinema for a minimum number of days per year to promote Korean culture and ensure that the continued viability of the Korean film industry. Current law requires that Korean films are shown 146 days of the year, with a potential reduction to 106 days. In 1998, the screen quota issue was being negotiated within the context of Bilateral Investment Treaty (BIT) negotiations.

DRAMs

The Department of Commerce issued an anti-dumping order on dynamic random access semiconductors (DRAMs) in 1993, but found that sales of DRAMs by LG Semicon and Hyundai had not been dumped during two following administrative reviews. During a subsequent review in 1996, Commerce denied requests for revocation by these two companies because Commerce was not satisfied that there was no likelihood of future dumping by these firms if the antidumping order was revoked, specifically noting the sharp decline in DRAM prices during 1996. Korea subsequently requested WTO dispute settlement consultations, and a panel was established in January 1998.

The WTO panel's final report was issued in January 1999. While rejecting most of Korea's arguments, the panel did find that Commerce's "not likely" standard for revocation was insufficient under the WTO Antidumping Agreement. However, the panel rejected Korea's request that it recommend revocation of the antidumping order as the appropriate method of implementing the panel's findings. The report has not yet been adopted by the DSB, and an appeal remains possible.

Airport Procurement

During negotiations on Korea's entry into the WTO Agreement on Government Procurement (GPA), the U.S. Government received assurances that procurement would be conducted by GPA-covered entities. Since 1997, U.S. companies have alleged that the Korean Airport Construction Authority (KOACA), which is responsible for managing procurement for Inchon Airport, discriminates against foreign firms interested in bidding for projects. KOACA procurement practices, such as short deadlines and domestic partnering requirements, are in violation of WTO GPA requirements and restrict the ability of U.S. firms to participate in bidding.

In 1997 and 1998, U.S. negotiators raised this issue in the WTO Government Procurement Committee and in consultations, including at the lighest levels. Korea's response has been to claim that KOACA is not covered by the GPA. As Korea's position on this issue remained unchanged, the U.S. Government delivered a request for consultations under the WTO on February 16..

India

General

Current U.S. trade and investment policy with India involves working through the WTO panel process two disputes (TRIPS mail box and BOP import licensing) and pressing our ever-present list of irritants (e.g., automotive TRIMS, soda ash restrictions, insurance and almonds market access) U.S. policy goals continue to be enhanced market access for goods and services, investment liberalization, and protection of IPR. India is a difficult market to access due to the lack of a stable political consensus for trade and investment liberalization and residual tendencies from previous economic regimes. The BJP government is going into the 1999/2000 fiscal year's budget process with a less than rosy economic performance for FY 1998/99 - GDP growth below 6%, reduced foreign investment inflows, and the gross fiscal deficit exceeding the target ratio of 5.6% of GDP causing increased GOI borrowing and inflationary pressures

BOP WTO Case

For consumer goods, a category broadly defined to cover about 3000 tariff line items, QRs are imposed by India that had been justified previously under WTO balance of payments provisions. The WTO Balance of Payments Committee was informed by the IMF in June 1997 that India does not have a BOP problem for which India needs to maintain its QRs. The BOP Committee was unable to come to the logical conclusion that India does not have a WTO BOP justification for these restrictions because India and several other developing countries blocked consensus.

The United States held WTO dispute settlement consultations with India in mid-September 1997 as well as bilateral discussions in late October, early November and December regarding the phase-out of these WTO-inconsistent measures. Despite considerable movement on the U.S. side, India was unable to match this flexibility to a degree that would produce a negotiated resolution superior to the adjudicated result of a WTO dispute settlement panel. While other major trading partners were willing to accept such a result, at the request of the United States a panel was established November 18. The interim report of the panel was issued in mid December 1998 and the final report is expected to be publicly available by March.

TRIPS Mail Box

India failed to implement statutorily in 1995 the patent protection-related "mailbox" provisions of the TRIPS Agreement, leaving India in violation of its TRIPS obligations in this area. In mid-1996 the United States initiated WTO dispute settlement proceedings on this issue and in August 1997 prevailed before a WTO panel, as well as before the WTO Appellate Body in mid-December, 1997. This decision represents a significant victory for the U.S. pharmaceutical and agricultural chemical industries and patent protection generally. However, India promulgated in early January 1999 a patent ordinance, in an attempt to fulfill its TRIPS obligation, that the USG find to be WTO-inconsistent due to the inclusion of compulsory licensing and other objectionable practices. The United States is seeking the modification of the ordinance and any superceding legislation or the reconvening of the WTO panel to rule on the consistency of the Indian measure.

Auto TRIMS

The Indian automotive regime is characterized by high applied tariffs, restrictive import licensing and WTO-inconsistent TRIMS (local content and export performance requirements). In late 1997, the Indian Government through the mechanism of the Cabinet Committee on Economic Affairs (CCEA), approved a comprehensive new auto policy. This policy set out in a more transparent manner the rules for foreign auto manufacturing investments, tied to import licenses for CKD and SKD vehicle kits, in MOUs between the foreign firms and the government. The new policy specifies that auto production facilities and not mere assembly operations must be established by foreign investors in the sector. Majority foreign partners in new joint ventures must have a minimum equity investment of US$50 million by the third year of the project; reach 50 % local content for components by the third year and 70% by the fifth year; and begin to implement its export performance requirements by the third year. From the fourth year until the termination of the MOU, the value of CKD and SKD kit imports may be regulated by the export obligations fulfilled in the previous year. The MOU obligations also stipulate production planning, and the achievement of a broad neutralization of foreign exchange over the time period of the MOU by balancing the outflow of foreign exchange on account of CKD and SKD kit imports and projected export earnings from intermediate and final automotive products.

The policy requires that all joint venture auto manufacturers enter into this MOU with the Directorate General of Foreign Trade in order to obtain import licenses for CKD and SKD vehicle kits. India did not notify these auto TRIMs and thus appears to be in violation of its WTO obligations. The United States, the EU and the Japanese have pressed India in two TRIMS committee meetings in 1998 and WTO dispute settlement consultations in December 1998 to reconcile these policies with their WTO obligations. The EU has requested a panel to review the WTO-consistency of these measures.

Financial and Telecom Services

While the Indians made some modest commitments in banking and securities in the WTO financial services negotiation, its insurance market access offer was not commercially useful. The USG has and will continue to press the GOI to improve its offer on insurance. The ruling BJP coalition attempted to introduce insurance reform legislation in December 1998 but only to see it sidetracked to a select committee in the face of violent street demonstrations instigated by the affected unions and Communist Party. Chances are slim for passage during the budget session of Parliament commencing in February of 1999. There is also a general lack of market access for telecom services, even though the GOI has issued periodic pronouncements promising liberalization. India’s participation in the WTO telecom services negotiations was uninspiring. The United States expects India to reduce limits on foreign investment, accelerate access to long-distance and international telephone services and improve adherence to the WTO basic telecom reference paper. (In response to pressure from domestic software producers, India has begun liberalizing access to supply Internet services.)

Investment

While the Government of India has taken useful steps to liberalize its investment regime since it inaugurated economic reforms in the early 1990's, additional steps are needed to facilitate India's infrastructure development.

Textiles

Both countries continue to restrict the importation of certain textiles and apparel from the other; the United States through the WTO Agreement on Textiles and Clothing and India by means of WTO-inconsistent bans previously justified under the

WTO BOP provisions. In December 1994, the United States and India signed a bilateral market access agreement, marking the first time that Indian import of U.S. textiles and clothing have been permitted. Immediate "unrestricted" access was provided to several key U.S. products -- including fibers, yarns and industrial fabrics. QRs are also scheduled to be lifted over the time period 1997 to 2002 for apparel fabrics, home furnishings and clothing. India also agreed to reductions in the tariffs levied on imports covering the entire range of textile products. In the year ending November1998, with four years of quota growth rate increases benefitting India under the Agreement on Textiles and Clothing, U.S. imports from India increased 9 percent to a level of over $2.3 billion or 1 billion square meters equivalent, placing India sixth in the ranking of U.S. import suppliers.

GSP

India frequently expresses interest in expanding coverage of GSP eligible products. However, many products of interest to India are excluded by statute, such as textiles, footwear, leather wearing apparel, and other import sensitive products. Some products, such as Indian chemicals and pharmaceuticals, lack eligibility because of India's failure to provide pharmaceutical product patent protection. The GSP subcommittee decided in December 1998 to accept for review the petition of the American Natural Soda Ash Corporation (ANSAC) to withdraw, suspend or limit the application of GSP treatment to Indian imports due to the lack of market access to the Indian market stemming from the injunction of the Indian Monopolies and Restrictive Trade Practices Commission barring ANSAC imports. Public hearing are scheduled for the latter half of March 1999.

The Association of Southeast Asian Nations (ASEAN)

U.S. trade with the nine ASEAN countries (Brunei, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam and Burma) declined in 1998, with estimated two-way trade falling by 6 percent ($7.2 billion) to $112 billion. ASEAN collectively continues to be the United States' fifth largest trading partner. Largely due to the Asian financial crisis, exports to ASEAN fell by an estimated 20 percent ($9.6 billion) to $38.6 billion.

In 1993, the then seven members of ASEAN created the ASEAN Free Trade Area (AFTA) as a means to promote regional economic competitiveness and prosperity. The objective of AFTA is to promote trade among ASEAN member countries by gradually reducing customs duties on intra-ASEAN trade of qualifying products by 2005, with special allowance for sensitive sectors. By agreement, AFTA members agreed to accelerate the reduction of tariff cuts under AFTA by 2003. Laos and Burma were admitted to ASEAN as full members in July 1997, although these countries have until 2008 to phase in obligations under the AFTA. Cambodia continues a dialogue with ASEAN members to become a full member of the regional organization, and integration into the AFTA. However, Cambodia's full membership in ASEAN continues to be postponed pending democratic reforms.

In recent years, ASEAN continued with efforts to implement and expand the AFTA by including unprocessed agricultural commodities in the tariff phase-out scheme, and placing greater emphasis on the elimination of nontariff measures such as customs surcharges and technical barriers to trade. During the December 1998 ASEAN Summit in Hanoi, leaders agreed to accelerate reduction of AFTA Common Effective Preferential Tariff (CEPT) rates to ensure that a minimum 90% of tariff lines are subject to 0-5% rates by 2000 (3 years ahead of schedule). They also agreed to expand the scope of products for which CEPT rates will be eliminated by 2003 (which accounts for roughly 83% of AFTA tariff lines). In recognition of their late accession to the AFTA, Vietnam, Laos, and Burma will follow a modified schedule. However, specific details regarding how each ASEAN member will implement these objectives is yet to be worked out.

ASEAN also intends to expand negotiations under the Framework Agreement on Services beyond the current priority areas with a view to eventually including all sectors and all modes of supply. The Hanoi Summit also produced the "ASEAN Vision 2020" declaration in which members resolved, among other things, to continue with full implementation of AFTA, to implement fully the ASEAN Investment Area (AIA) by 2010, and to achieve the free flow of investment by 2020. The eventual creation of ASEAN patent and trademark offices are longer-term goals, however, efforts toward coordinating documentation and application filing procedures continues.

Indonesia

General: Due to the economic crisis and political upheaval in Indonesia for the past year, bilateral trade issues have not commanded the undivided attention of the Indonesian Government. Some observers believe that Indonesia's economy may be at its bottom, having completed 1998 with a GDP contraction of 13% and inflation of 77%, with concomitant unemployment and food price/distribution problems. While the Indonesian authorities have made some progress in implementing economic and political reforms needed to restore confidence, the economy appears to continue to lack the confidence and political certainty necessary for recovery. Indonesia's program with the IMF, initiated in October 1997, has been modified several times since then as the economic situation deteriorated. In June 1998 the program was adjusted to allow for greater fiscal expenditures to help blunt the impact of the crisis on Indonesia's poorest and ensure their access to needed food, fuel, and medicine. There are continuing and serious problems in Indonesia's financial and corporate sectors.

IPR Protection: Despite some progress, Indonesia is on the USTR special 301 Priority Watch List for 1998 due to continuing problems raised by U.S. industry. These include software, book, video, VCD, drug, and apparel trademark piracy; audiovisual market access barriers; inconsistent enforcement and an ineffective legal system; and amendments to the copyright, patent and trademark laws that are not completely TRIPS consistent. These issues had been raised with the GOI in the past year, although the focus in Indonesia during that period has been primarily attaining economic and political stability. Because of this turmoil, USTR was able to present only in late June an IPR work plan (market access, enhanced enforcement, TRIPS consistency of laws, special juridical arrangements, legal GOI use of software, and increased protection of well-known marks including several company-specific cases) with the proposal that if these changes are implemented by December 1998, USTR would review the situation to see if a change in list status is warranted. The Indonesian Government has yet to take sufficient action on the proposed work plan that would get them to the watch list. The GOI has acknowledged the need for improved enforcement and a broad education program, in addition to the need to bring its statutes into TRIPS conformity.

Worker Rights/GSP): As a result of insufficient progress in promoting worker rights the USG denied in 1998 GSP benefits for seven Indonesian products valued at $12.7 million and in 1997 for six items also with a small trade value. Indonesia passed a new labor law in September 1997 containing a number of positive elements, and in November 1997 USTR initiated a dialogue with the GOI by means of an action plan to secure further progress. The action plan has benchmarks on worker rights focusing on freedom of association and the rights to organize and bargain collectively. Since its proposal, the USG received some useful responses from the GOI but not enough worker rights progress to warrant granting the de minimis waivers during the May 1998 GSP review.

Before the political upheaval of May 1998, problems clearly existed in Indonesia's worker rights regime. These included the questionable independence of the unions in relationship to government, the Ministry of Manpower involvement in union dues collection, and police and military involvement in labor matters. However, since then Muchtar Pakpahan and other political prisoners have been released, and there is currently the potential for greater reform of Indonesian law and practice as it affects the right to associate and bargain collectively. ILO convention 87 on the right of association was ratified by Soeharto's successor, President Habibie, and unions, including Pakpahan's SBSI, have been permitted to organize and to register. The previously government-controlled SPSI has split, with a majority, reformist wing emerging that is trying to act like a real union. The impediments at this juncture are old attitudes and behavior in parts of the bureaucracy and a conflicting overlay of old laws and presidential decrees on top of new decrees, in which the last category of more progressive regulations technically may not take legal precedence. There also appears to be continued military interference in organizing and strikes. The USG presently is evaluating the situation and continuing the discussions as the GSP review cycle proceeds.

IMF Trade-Related Conditionality: Indonesia's initial October 31, 1997 Memorandum of Economic and Financial Policy (MEFP) with the IMF has been revised several times in response to deteriorating macroeconomic conditions. The latter versions of the program expanded the focus of earlier programs to cover the entire range of economic challenges facing Indonesia. These include fiscal policy, monetary policy, structural reform and deregulation, corporate debt and bankruptcy proceedings, banking sector reform and restructuring, restoration of trade financing to promote exports, food security, the distribution system and social safety net policies. In accordance with the IMF program, the Indonesian authorities are taking initial steps to restructure the banking system and to facilitate the restructuring of corporate debt burdens.

The IMF memoranda contain a considerable amount of trade-relate conditionality that if fully implemented by the GOI will contribute to significant liberalization of the real economy and reduction of distortions in the Indonesian goods and services markets. Despite the sharp economic downturn in Indonesia, the Indonesian Government has undertaken structural reforms to dismantle the national car and aircraft programs, reduce tariffs on agricultural commodities and industrial goods, eliminate export taxes, and disband marketing monopolies. Indonesia appears to be implementing its border liberalization and internal market reforms captured in the IMF memoranda from last October to date, although careful monitoring is warranted given the ambitious scope of liberalization involved and the relatively low level of commercial activity this year.

Automobiles: By virtue of the successful challenge by the U.S.(in addition to the EU and Japan) of the WTO consistency of Indonesia's auto policies, Indonesia must bring its auto policies into compliance with the panel ruling. The final report of the WTO dispute settlement panel examining Indonesia's auto programs constitutes a significant victory for the United States in its effort to dismantle Indonesian barriers to trade in automotive products. It also serves as an important precedent in combating similar barriers in other markets.

The WTO panel issued its final report in June 1998. The panel ruled in favor of the United States in its challenge to various measures taken by Indonesia that hinder market access for U.S. automotive products. The panel found that the provision by Indonesia of local content subsidies under both its 1993 Program and its National Car Program violates Article III of the GATT and Article 2 of the Agreement on TRIMs. The panel also found that the extension of certain of these subsidies to automobiles imported from Korea violates Article I of the GATT. When this panel ruling is implemented by the Government of Indonesia, the various policy elements that conferred the benefits associated with " National Car" status will be addressed and removed as a barrier to U.S. exports.

The Government of Indonesia wrote to the WTO Dispute Settlement Body (DSB), as well as to the three complainants, that Indonesia will fully comply with the recommendation and rulings of the DSB adopted on July 23, 1998. The communication further stated that the February 1996 car program had been revoked on January 21, 1998 and that Indonesia would meet its WTO obligations with regard to the 1993 car program no later than October 23, 1999. The Government of Indonesia has further specified in writing that the Indonesia firm intended to be the producer of the national car, PT Timor, will be required to reimburse the Government of Indonesia for the import duties and luxury taxes owed on the Kia sedans imported from Korea. On October 6, the EU requested WTO arbitration to determine the reasonable time period of implementation of the DSB rulings on the 1993 program. The United States participated in the arbitration process that resulted in the recent ruling that Indonesia must implement fully by July 23, 1999, or twelve months from the date of the panel report adoption.

Malaysia

Economic Climate: In reaction to the economic crisis, the Malaysian Government in September 1998 imposed an array of capital controls to insulate the Malaysian economy, including restrictions on the convertibility of Malaysian currency (Ringgit) outside the Malaysian economy, a one-year freeze on the movement of portfolio investment out of Malaysia, limits on the amount of Ringgit which residents and foreigners may bring in to or take out of Malaysia, central bank approval for various internal and foreign transfers, and the requirement that exports must be financed in foreign currency. These measures may have lead to a reduction of foreign direct investment in Malaysia. A decline in foreign investment is likely to have secondary effects in contributing to the decrease of Malaysia's export and import levels beyond the suppression of import demand resulting from the crisis and devaluation of the Ringitt.

Investment and Services: Malaysia maintains investment limits which pre-date the crisis and which affect the local business and investment climate. In general, Malaysian law requires that business entities include a domestic partner with a minimum 30 percent stake. Banking and other financial services providers face foreign-held equity restrictions, as do suppliers in the wholesale/retail, distribution and multi-level marketing, construction and legal services sectors. United States officials have raised concerns over investment restrictions in the distribution services sector as a priority and continue to monitor developments.

Tariffs: In 1997 and 1998, Malaysia raised tariffs on certain goods from 0 percent in 1996 to current levels of between 5 and 20 percent ad valorem. The products affected include some types of heavy machinery and construction equipment, automobiles, motorcycles, and home appliances. Malaysia in 1998 also implemented a new import approval scheme for construction equipment which could further restrict market opportunities for U.S. exports. Malaysia's rationale for the measures affecting construction equipment is to encourage reconditioning and repair of existing equipment; however, it is unclear that this policy has promoted this objective. Malaysia is reducing tariffs for information technology products covered by the Information Technology Agreement (ITA), under which tariffs will be bound at zero by the year 2000.

Local Content-Related Investment Incentives: Malaysia has taken a number of steps which confer tariff or tax benefits, based on the amount of locally produced parts or inputs utilized, in order to promote the development of domestic automobile manufacturers under its "national automobile" program. As required by the WTO Agreement on Trade-Related Investment Measures (TRIMs), Malaysia's various incentives for local production are to be eliminated by January 1, 2000. The United States continues to closely monitor developments in the autos sector.

Intellectual Property Rights: The Malaysian Government has worked closely with U.S. industry to suppress end-user piracy of copyrighted works, principally business application software. However, Malaysia has not made effective efforts to regulate optical disk (OD) production facilities or to address the dramatically increasing problem of pirated CDs, VCDs and CD-ROMs. Domestic production of optical disks far exceeds domestic demand, and has contributed to substantial domestic and export markets for pirated goods. The United States continues to reiterate concern over these developments and urges Malaysia to make effective OD plant regulation a top priority.

Philippines

Market Access Issues: Despite the newly installed Estrada administration's articulated objective to resist domestic protectionism, and to maintain open-market policies to promote competitiveness and stability, the Philippine Government in 1998 considered a number of proposals to restrict import competition by means of increased taxes, surcharges and tariff increases. The Philippines in early 1999 raised applied tariffs on a range of goods of importance to the United States. At the same time, the Philippine Government has imposed product standards in at least one area where there has been no prior concern over consumer health or safety. U.S. companies and exporters have also observed an increase in the frequency of problems involving customs valuation and preshipment verification of invoice value for a range of agricultural and manufactured goods. As a signatory to the Information Technology Agreement (ITA), the Philippines is implementing tariff reductions for covered products which will be bound at zero by the year 2000.

Intellectual Property Rights: In June 1997, the Philippines enacted a comprehensive law on intellectual property rights (IPR). The law entered into force on January 1, 1998, although formal implementing regulations for most provisions of the law were not promulgated until later, and the Philippine Government has yet to issue regulations to implement copyright provisions of the law. On balance, the law represents a significant step toward implementation of the Philippines' commitments under the WTO TRIPS Agreement. However, several provisions of the law are of concern to the United States and could pose serious policy implications and investment disincentives if not adequately addressed through implementing regulations. Specific concerns include provisions governing the circumstances under which decompilation of software programs is permissible, ex parte search and seizure, and restrictions on technology licensing arrangements. The United States also continues to monitor carefully Philippine enforcement efforts and judicial efficiency.

Customs: Many U.S. companies have identified customs valuation and price verification practices as the single largest impediment to transacting business in the Philippines. In April 1996, the Philippines enacted legislation abolishing the use of the Philippines' previous customs valuation practice based on "home consumption value" (HCV). Similar concerns are expressed regarding implementation of the new valuation scheme (based on the "Brussels Definition of Value") which lacks transparency and may be inconsistent with the WTO Agreement on Customs Valuation. U.S. companies also report continuing problems with price verification procedures as part of the preshipment inspection (PSI) process, including routine overvaluation or "up-lift" of invoice prices without substantiation, failure to provide required customs documentation, questionable grievance and appeals procedures, and solicitation of "facilitation" fees not related to the services rendered. The United States continues to urge Philippine authorities to facilitate rapid implementation of the WTO Agreement on Customs Valuation and adherence to WTO PSI requirements.

Singapore

Singapore imposes tariffs on only four categories of goods, allowing nearly 96 percent if imports to enter duty-free. Singapore's tariffs on products covered by the Information Technology Agreement (ITA) will be bound at zero by the year 2000.

One aspect of Singapore's trade regime which remains to be a concern for the United States is the protection of intellectual property rights (IPR). Although Singapore during the past year has acceded to the Berne Convention, revised several IPR laws in order to become TRIPS-complaint in advance of the January 1, 2000 deadline, and has stepped up enforcement and consumer awareness efforts, Singapore's piracy rate continues to grow. Government efforts to promote a "code of conduct" for local manufacturers of optical disks in order to clean up the domestic industry has helped to focus attention on the growing problem of piracy of CDs, VCDs, and CD-ROMs. However, the non-binding and unenforceable nature of this "code" and the lack of efforts to strengthen border enforcement of intellectual property rights have not curtailed retail piracy of optical media.

Thailand

Intellectual Property Rights: In recent years, Thailand's commitment to effective IPR protection has been uneven, as evidenced by growing piracy rates, inconsistent coordination between enforcement authorities and failure to enact TRIPS-consistent patent and trademark laws. Thailand opened specialized IPR and international trade courts in late 1997 which has resulted in moderate improvements toward IPR protection, but has resulted in the imposition of deterrent penalties. In June 1998, the U.S. and Thailand concluded an Action Plan, which among other things, is intended to enhance routine coordination among relevant Thai Government agencies in order to improve retail-level IPR enforcement and to prioritize the enactment of key legislation. The Action Plan also sets the foundation for implementation of measures to address the growing problem of optical disk (OD) piracy. The United States will continue to monitor the situation in conjunction with U.S. industry.

Market Access Issues: Thailand's applied tariffs are generally higher than many of its neighbors. As a signatory to the Information Technology Agreement (ITA), Thailand is implementing tariff reductions for covered products which will be bound at zero by the year 2000. Thailand maintains a number of excise taxes which raise costs and reduce the competitiveness of U.S. exports. Moreover, Thailand's customs procedures lack transparency, are not consistently applied at all points of entry, and can be time-consuming and costly. Collectively, these inefficiencies artificially impede the free flow of imports and exports.

Worker Rights: Since 1992, the Thai worker rights situation has been the subject of an ongoing investigation under the Generalized System of Preferences (GSP). Of specific concern to the United States is the failure of successive Thai Governments to enact legislation which confers internationally-recognized labor rights to state enterprise workers. In late 1998 the Thai Parliament enacted the State Enterprise Labor Relations Act (SELRA), however, a court deemed technical aspects of the law to be inconsistent with provisions of Thailand's constitution which was revised that same year. The Thai Government has subsequently introduced a modified bill, intended to satisfy constitutional requirements, which continues to move through the Thai legislative process. The United States is hopeful that SELRA will be enacted and the GSP review can be satisfactorily concluded.

Vietnam

Good progress was made in 1998 in the process of normalizing trade relations with Vietnam continued in 1997. Negotiations of a bilateral trade agreement, which is a necessary precondition for Vietnam to receive normal trading relations status (i.e., formerly "most favored nation") from the United States under U.S. trade laws, moved forward. The United States seeks an equitable and mutually beneficial agreement which demonstrates Vietnam's movement toward WTO and other international norms in the conduct of its trade policies, and which serves to facilitate commerce between the two countries.

In April 1998, Vietnam submitted a trade agreement proposal which included provisions in all key areas raised by the United States: market access for goods, intellectual property, market access for services, and investment. This proposal was followed by a round of negotiations in Washington, at which a number of substantive differences between the two sides were identified. After subsequent review of positions, a second round of negotiations was held in September in Hanoi, at which a further narrowing of issues was achieved. Both sides are now preparing for another round of talks in the first quarter of 1999.

A second significant development in U.S-Vietnam trade relations in 1998 was the granting of the "Jackson Vanik" waiver by the President in March, and its renewal, required by law, in June. The "Jackson-Vanik" waiver, which requires that a country be making progress in allowing free emigration, is a prerequisite for normal trading status (along with the conclusion of the bilateral trade agreement). The waiver also is required to permit OPIC and EXIM programs, which are also important to U.S. trading interests, proceed.

Finally, in December, the President signed a Proclamation that allows the U.S.-Vietnam bilateral copyright agreement to enter into force. The President proclamation came after the issuance of regulations in Vietnam that clarify Vietnam's ability to implement the provisions of the agreement. Entry into force of the agreement, which occurred on December 23, means that U.S. copyrighted works now have legal protection in Vietnam for the first time.

Taiwan

Trade relations with Taiwan continue to be heavily influenced by on-going discussions about Taiwan's prospective entry into the World Trade Organization (WTO). In order to qualify for entry into the WTO, applicant countries must meet standards agreed to in the 1995 Uruguay Round of tariff negotiations. Taiwan completed its bilateral market access negotiations with the United States on February 20, 1998. Subsequent discussions with Taiwan in the WTO-context have centered on removal of WTO-illegal subsidies, access for U.S. motorcycles, as well as issues involving U.S. lawyer working in Taiwan.

Taiwan's bilateral agreement with the United States, which includes both immediate market access and phased-in commitments, will provide substantially increased access for U.S. goods and services and agriculture exports to Taiwan, our seventh leading export market. (In the agricultural area, substantial new access has been provided by Taiwan since June 1998 for U.S. pork, chicken, and other meat products.

Highlights of the 1998 bilateral WTO agreement included commitments by Taiwan to:

- reduce its overall tariff rates below 5%;
- reduce tariffs and discriminatory taxes of imported automobiles;
- open trade in the full range of products including chemicals, medical equipment; furniture, toys, steel, paper, construction and agricultural equipment, wood, civil aircraft, and distilled spirits;
- open Taiwan telecommunications services so that foreign companies can hold controlling interest and reduce excessively high interconnection charges for new telecom companies;
- accede to the WTO's Government Procurement Agreement and establish new arbitration procedures for resolving disputes involving major projects undertaken by the Taiwan authorities;
- remove import bans on pork, chicken, variety meats, and rice, as well as to provide immediate access for most of these products.

All countries which asked to negotiate bilateral agreements with Taiwan have concluded these agreements. Canada, however, has reopened in negotiations, and is requesting immediate access for pork and chicken products. The European Union is included among the list of countries that have concluded bilateral agreements.

The WTO expects to convene a Working Party in early to mid-1998 to review progress toward accession.

Intellectual Property Rights

Taiwan has made significant progress over the last several years in curtailing piracy of intellectual property. Retail raid on those selling pirated products have increased, court procedures tightened, and stiffer criminal penalties imposed. Taiwan companies have also pledged to eliminate investment in illegal IPR activities in other countries.

Nevertheless, significant problems remain. The United States has concerns about the effectiveness of Taiwan's efforts to suppress CD piracy and the export of counterfeit CDs, the integrity of Taiwan's patent system, as well as the difficulty of bringing successful legal actions against patent and copyright infringers.

Major Taiwan computer-chip manufacturers are moving toward final agreement on a system to mark all chips with identifying data. Initiation of such a program should make it much easier to find and prosecute video game piracy in Taiwan.

Medical Equipment and Pharmaceuticals

The administration by Taiwan of its national medical coverage program has raised numerous problems for foreign companies. Specifically, the Taiwan Ministry of Health has been unwilling to authorize payments for medical equipment above the most basic level of technology. Some progress toward resolving these issue was made in 1998, especially with regard to orthopedic implants. However, there is a need for further progress during 1999.

Cable TV

There has been a significant deterioration in the competitive environment within the Taiwan Cable TV market during the last year. U.S. program providers, which had previously sold to two competing cable systems, now were forced to sell to a single buyer in the Taipei market. As a result, U.S. program providers received much lower prices than they had earlier. New legislation is pending before the Taiwan Legislative Yuan. This legislation, if passed, could improve the competitive environment.

Hong Kong (Special Administrative Region)

Intellectual Property Rights (IPR)

Hong Kong has exerted strong efforts during the last year in combating IPR piracy. More resources have been devoted to curbing retail piracy, and major pirate markets have been closed for periods of time. New legislation was passed and implemented giving Hong Kong Customs officials the power to license and inspect CD production facilities. The Hong Kong public has also become much more aware of the damage being sustained by its own industries, notably movies and toys, from pirates. The United States has urged Hong Kong to continue to make the necessary resources available to combat IPR piracy.

Telecommunications

Hong Kong has made substantial progress in opening telecommunications markets. The last step -- opening the local and international phone market to companies which build facilities in Hong Kong -- has proven the most difficult. Hong Kong is now debating how much it can open the facilities-based market to new international investors. New infrastructure licenses would bring much needed investment into Hong Kong, and would ensure that Hong Kong remains a premier business center in the Asian-Pacific region.

People's Republic of China

The framework for U.S. trade relations with China is based on a bilateral trade agreement that first took effect February 1, 1980. The Agreement extends normal trade relations (NTR) treatment to exports from both countries, contains safeguards against market disruption, and commits both parties to protect intellectual property. The Agreement is subject to renewal at three-year intervals, but all or part of the Agreement may be suspended if a party lacks domestic legal authority to implement it. The most recent renewal of the Agreement was on February 1, 1998.

China's receipt of NTR tariff treatment is reviewed on an annual basis. To extend NTR treatment, the President must waive Section 402 of the 1974 Trade Act, the Jackson-Vanik Amendment. The President last notified Congress of his decision to waive Jackson-Vanik and permit NTR renewal for China on June 3, 1998; he must decide by June 3, 1999, whether to waive NTR for another year. While pledging in 1994 not to base renewal of NTR on China meeting specific human rights conditions, the President committed his Administration to addressing unfair trade practices aggressively, as well as other issues.

Intellectual Property Rights

Since 1986, the United States and China have engaged in detailed discussions regarding the improvement of China's protection of intellectual property. These discussions have covered copyright, patent, trade secret and unfair competition, and semiconductor layout design and trademark laws, as well as the enforcement of those laws. The United States and China have also discussed customs enforcement and technical assistance issues.

As the result of an investigation under the "Special 301" provisions of the 1988 Omnibus Trade and Competitiveness Act (1988 Act), the United States and China reached an agreement on January 17, 1992, on improved protection for U.S. inventions and copyrighted works, including computer software and sound recordings, trademarks, and trade secrets. In 1995, the United States and China signed the Intellectual Property Rights Enforcement Agreement. In June 1996, the two countries signed an accord, which reported on enforcement actions taken under the terms of the 1995 Agreement and market access issues. Discussions over the past year have also focused on implementation of the WTO Agreement on Trade-Related Aspects of Intellectual Property (TRIPs) as well as specific IPR enforcement issues.

Improvements in Intellectual Property Rights Standards

Copyrights

China joined the Berne Convention and the Universal Copyright Convention on October 15, 1992, and the Geneva Phonogram Convention on April 30, 1993. These have led to improved levels of protection accorded copyrighted works, especially computer software and sound recordings. China continues to issue new regulations to implement these treaties. China has proposed revisions to its copyright law to bring it into conformity with the requirements of the TRIPs Agreement. This would also be an opportunity for China to implement two copyright related agreements negotiated under the auspices of the World Intellectual Property Organization (WIPO) that China has signed but not yet ratified.

Patents

China amended its patent law to, *inter alia*, protect products and processes for all chemical inventions, extend the term of protection from 15 to 20 years from the date of filing, and include restrictions on the grant of compulsory licenses. In addition, China has issued regulations to provide administrative protection for U.S. patented pharmaceuticals and agrochemicals. China joined the Patent Cooperation Treaty on January 1, 1994.

Trademarks

China is a member of the Paris Convention for the Protection of Industrial Property. On September 1, 1995, China acceded to the Madrid Protocol on the Protection of Marks. Several trademark laws and implementing regulations have since been adopted to adapt to China's laws to comply with the Madrid Protocol. Trademark protection, particularly for unregistered well-known trademarks, is an important part of our bilateral discussions. China is now in the process of revising its trademark law and regulations to improve implementation of its international obligations, including those that would apply under the TRIPs Agreement

Trade Secrets

In fulfillment of its commitment in the 1992 IPR Agreement, China passed an Unfair Competition Law that improves protection for trade secrets. In 1995, China also promulgated regulations on the protection of business secrets.

Enforcement of Intellectual Property Rights

Although China improved its intellectual property laws after 1992, enforcement of these laws was poor, especially with regard to copyrighted works. In 1994, USTR initiated a Special 301 investigation into China's enforcement practices and lack of market access for U.S. companies. As a result, in 1995, the United States and China signed the Intellectual Property Rights Enforcement Agreement which provides for improved protection for copyrights, strengthened border controls, instituted trademark law modernization, and obligated China to intensify a "Special Enforcement Period" aimed at cracking down on piracy. The enforcement agreement also obligated China to open its markets to legitimate audiovisual products by eliminating quotas and other market barriers.

USTR has closely monitored the implementation of the 1995 Agreement. As part of that process, other agencies, including the Department of Justice, the

Federal Bureau of Investigation, the U.S. Customs Service, and the Patent and Trademark Office of the Department of Commerce, provide technical assistance to Chinese authorities to improve their ability to protect intellectual property. In June 1996, the United States and China reached an accord outlining the steps China took to implement the 1995 Agreement and to provide more detailed market access guidelines.

Chinese enforcement of copyrights and trademarks is still uneven from province to province. Of particular concern is the significant level of unauthorized use of software by both private enterprises and government ministries (end user piracy). Piracy rates of entertainment software (game compact discs) and other audiovisual products are also very high. Industry sources also report increasing problems with trademark counterfeiting. U.S. goods have now entered China's market, and had an opportunity to develop a reputation for quality, which makes them a target for counterfeiters.

Access for foreign sound recordings has improved, but restrictions on distribution remain a key concern. Although imports of foreign video titles have increased rapidly, the Chinese still impose an unofficial quota on foreign motion pictures that are distributed on a revenue sharing basis. China maintains this limit through a state-owned import monopoly. We will continue to seek market access, including distribution rights, for the audiovisual sector in China's WTO accession negotiations.

Market Access Agreement

The United States and China signed a Memorandum of Understanding (MOU) on Market Access in 1992. This Agreement committed China to changes in its import regime implemented over a five year period, including increased transparency, elimination of quotas and licenses, a guarantee that no trade law or regulation could be enforced unless published, uniform application of trade rules, elimination of import substitution policies and a ban on the use of standards as barriers to trade. While China has phased-out formal measures, such as quotas and licenses, non-uniform application of trade rules, import substitution policies and use of sanitary and phytosanitary standards to restrict imports remain serious problems.

The use of non-transparent, duplicative and discriminatory standards and or licensing requirements is also common. The Department of Commerce in late 1997 initiated a program under the Joint Committee on Commerce and Trade to improve China's standards setting system for key U.S. industries.

Although China agreed in the 1992 MOU to base its sanitary and phytosanitary measures on sound science, China maintains restrictions on many agricultural imports based on questionable scientific grounds, especially for citrus, Pacific Northwest wheat, meat, plums and tobacco. Nor does China consistently recognize standard international practices, such as those contained in the WTO Agreement on the Application of Sanitary and Phytosanitary Measures. For example, China continues to prohibit all imports of U.S. citrus, without regard to strict quarantine procedures or the existence of pest-free areas. We are seeking to resolve these issues as soon as possible.

China continues to reduce tariffs in line with its APEC commitment to limit overall tariffs to 15 percent by the year 2000. China reduced its overall tariff level to around 17 percent in 1997 and announced further reductions again in early 1999; however, some tariffs on priority products remain quite high or were actually raised. Although China committed in 1997 to implementing the Information Technology Agreement as soon as possible, it has yet to join that Agreement. Obtaining binding tariff commitments on products of priority interest to the United States is a key issue of the bilateral market access talks in China's WTO accession.

In 1998, in large part reflecting the efforts of the Asia financial crisis, China has begun to consider and, in some cases, implement measures designed to insulate some domestic markets from international competition. For example, new measures affecting pharmaceuticals, telecommunications and energy generation have been considered and in some cases implemented.

WTO Accession

Negotiating commercially meaningful terms for China's accession to the WTO was a major focus of the Administration's trade policy in 1998. Intensive negotiations took place over the past year particularly in connection with the President's visit to China in June 1998.

WTO negotiations include two main areas. First, members of the Working Party on the Accession of China negotiate bilaterally to obtain market access commitments on tariff rates and elimination of nontariff measures (i.e., quotas, tendering and licensing) for industrial and agriculture products and progressive liberalization for services (e.g., distribution, professional, telecommunications, financial, audiovisual services). Broadly defined, market access negotiations also address other measures, such as performance requirements, standards and sanitary and phytosanitary measures that act as barriers to market entry. These commitments are applied on a most-favored nation (MFN) basis (now called normal trade relations (NTR) in U.S. law) and will form an integral part of China's WTO Agreement.

In 1998, China and members of the Working Party continued to focus on the market access part of the negotiation with particular attention to tariffs, nontariff measures and market access for services. While progress has been made, considerable work remains, especially on services, agriculture and some industrial products.

Second, members of the Working Party negotiate multilaterally to commit China to conform its current trade regime in accordance with WTO principles and obligations, such as those pertaining to national treatment, non-discrimination, transparency, balance-of-payments, safeguards, subsidies, standards, customs valuation, state-trading and price controls. China's terms of accession are set forth in legally-binding documents called the protocol of accession and the Working Party report. After a Working Party consensus is reached on the draft documents, they are transmitted to the General Council which must approve China's accession by a two-thirds vote of all WTO members.

To date, China has agreed to the resolution of some key protocol issues, including nondiscrimination, uniformity of trade rules, the right of judicial appeal of administrative decisions related to trade, and the application of the Agreement on Trade-Related Intellectual Property Rights.

Satellite Launch Services

On March 13, 1995, the United States and China agreed to extend the Bilateral Agreement on International Trade in Commercial Space Launch Services. The Agreement was intended to balance the interests of the U.S. satellite and commercial space launch industries while encouraging free trade by allowing China to enter the international market for commercial space launch services in a fair and non-disruptive manner. The Agreement covers the period from 1995 to 2001 and continues quantitative and pricing disciplines established under the first U.S.-China space launch services agreement signed in 1989. The renewed Agreement initially limits China to 15 launches over this time period. An increase in the GEO launch limit, up to a potential of 20 launches, may be triggered as a result of stronger than predicted growth for GEO launch services. With respect to the low earth orbit (LEO) satellite launch market, the Agreement requires that Chinese participation in the LEO market segment be proportionate and non-disruptive. Both the GEO and LEO launches are to be priced on a par with other Western providers. The Space Launch Services Agreement specifically provides that nothing in the Agreement limits the operation of U.S. export control laws.

As a result of a 1997 determination that the pricing terms of one of the contracts for a GEO launch was not consistent with the provisions of the Agreement, the United States decided not to consider exercising any discretionary increase at that time in the limitation launches to GEO provided for in the Agreement beyond the original 15. Chinese launch providers conducted four commercial launches to LEO and none to GEO in 1998, for an 11 percent share of the worldwide commercial launch services market. U.S. launch providers conducted 17 commercial launches in 1998, for a 47 percent share of the worldwide commercial launch market. The United States will continue to monitor the prices, terms and conditions offered by Chinese launch services providers during the bid stage of international commercial competitions.

Japan

In 1998, the Clinton Administration continued its intensive and sustained efforts to remove substantial barriers to market access for U.S. goods and services, promote urgently needed deregulation, and enhance the operation of pro-competitive mechanisms throughout the Japanese economy. The Administration pursued these trade policy objectives through a wide variety of bilateral negotiations and consultations, and multilateral fora, including the World Trade Organization (WTO) and Asia Pacific Economic Cooperation (APEC) forum. Throughout the year the United States also consistently emphasized the critical need for Japan to adopt prompt and effective fiscal stimulus and banking reform, fundamental deregulation, and meaningful market-opening measures in order to achieve renewed and sustained growth of the Japanese economy, experiencing its worst recession in postwar history.

The Clinton Administration focused considerable time and attention in 1998 on monitoring and enforcing the 35 trade agreements concluded with Japan since 1993, particularly with respect to insurance, flat glass, autos and auto parts and government procurement. As elaborated below, the United States and Japan reached two new trade agreements in 1998 in which Japan pledges to deregulate its economy in critical areas, such as telecommunications, housing, financial services, and medical devices, and to significantly expand air service across the Pacific.

Despite the severe economic conditions in Japan, the United States achieved progress in opening Japan's market in 1998, particularly with respect to telecommunications, medical technology and semiconductors. Nevertheless, trade tensions grew between the two countries as the United States faced a surge in steel imports from Japan and the bilateral trade deficit for 1998 reached $64.1 billion, up 14 percent from 1997.

The highlights of our 1998 bilateral and multilateral trade agenda with Japan are as follows:

Overview of Accomplishments 1998

The United States made further progress in promoting comprehensive deregulation in Japan in 1998. Under the Enhanced Initiative on Deregulation and Competition Policy (Enhanced Initiative), Japan agreed in May to take a number of significant deregulatory steps in the telecommunications, housing, financial services, and medical devices/pharmaceutical products sectors and to add energy as a fifth sector covered under the Enhanced Initiative. Japan also agreed to implement specific measures to address structural concerns relating to competition policy, distribution, and transparency. In addition to pressing Japan to fully implement these deregulatory measures, the United States built on the accomplishments of the first year of the Enhanced Initiative by submitting to Japan in October more than 200 proposals aimed at further deregulation of the Japanese economy. These proposals expand upon those measures already agreed to in the first year and include new deregulation measures in the sectoral and structural areas covered under the Enhanced Initiative.

The United States also concluded a Civil Aviation Agreement with Japan in January. This agreement is aimed at significantly liberalizing the civil aviation market between the United States and Japan, including for both U.S. passenger and cargo carriers, and is expected to increase U.S. aviation service-related exports by $1 billion annually.

The Administration continued to place a high priority in 1998 on the monitoring and enforcement of existing agreements to ensure their successful implementation. Both the Office of the U.S. Trade Representative and the Department of Commerce significantly increased their resources dedicated to this effort and a significant number of U.S. Government officials met with their Japanese counterparts throughout the year to discuss progress under important bilateral agreements, including: autos and auto parts, insurance, flat glass, government procurement of computers, supercomputers, medical technology, telecommunications, and construction.

In addition, the Administration also released its first semi-annual film monitoring report in August. The report reviewed formal representations made by Japan to the World Trade Organization (WTO) regarding its efforts to ensure the openness of its photographic film and paper market. While the report showed improvements in market access within some sectors of the market, it called on Japan to take additional action to open its photographic film and paper market and to ensure the elimination of practices that unreasonably restrict competition in this sector.

Further, the United States continued to use the WTO Dispute Settlement Mechanism to address market access barriers in Japan. In October, a WTO dispute panel ruled in favor of the United States in its case against Japan regarding its unfairly burdensome and discriminatory requirements on varietal testing of fruits exported to Japan. The WTO ruled that these requirements have no apparent scientific basis. Both parties appealed this decision and in February 1999 the WTO Appellete Body upheld the panel's findings in favor of the United States.

Deregulation

On May 15, 1998, President Clinton and then-Prime Minister Hashimoto announced in Birmingham, U.K. the First Joint Status Report under the Enhanced Initiative. This report documents the deregulation measures Japan agreed to take in a number of key sectoral and structural issues during the Enhanced Initiative's first year. The Enhanced Initiative, announced by the President and Prime Minister in June 1997 at the Denver G-8 Summit, established a bilateral forum for addressing deregulation and market access issues in Japan. Initially, the Enhanced Initiative focused on addressing market access and regulatory issues in four important sectors: (1) Telecommunications; (2) Housing; (3) Financial Services, and (4) Medical Devices and Pharmaceuticals. At Birmingham, the Energy sector was added to this list. These sectors were chosen because of their economic importance to U.S. industry, as well as their effect upon the overall global competitiveness of U.S. companies operating in these sectors. The Enhanced Initiative also addresses the critical cross-cutting structural issues of Competition Policy, Distribution, and Transparency.

Recognizing that deregulation is an ongoing process, and building on the accomplishments achieved at Birmingham, the United States transmitted to Japan in October 1998, a submission containing over 200 proposals for further deregulation in the sectors and structural areas covered under the Enhanced Initiative. Highlights of the achievements in 1998, and key U.S. proposals for further progress in 1999, are as follows:

Sectoral Deregulation

Telecommunications Deregulation:
Over-regulation and restrictive practices by Japan's incumbent telecommunications carriers have stifled competition and slowed growth in Japan's $128 billion broadcasting and telecommunications services market. As a result, new investment in this sector is declining and Japan's telephone rates remain much higher than those in other markets.

Under the first year of the Enhanced Initiative, Japan agreed to adopt a new regime to lower the rates that telecommunications carriers must pay to connect to Japan's local telecommunications network (reduction in interconnection rates). When implemented in the target date of the year 2000, the long run incremental cost methodology (LRIC) which eliminates unjustified costs from interconnection should dramatically increase competitive opportunities. Prior to implementation of LRIC, Japan committed to reducing interconnection rates as much as possible. If interim rates fall significantly, this should improve competitive conditions.

Japan has also agreed to introduce measures designed to facilitate access to land and physical facilities, such as those relating to access to public roads by new market entrants constructing new networks. In addition, Japan has agreed to liberalize its international services market by permitting companies to provide alternatives to traditional international service. These steps should reduce the huge fees U.S. carriers now pay to Japanese carriers, encourage new entrants into the Japanese market, and result in hundreds of millions of dollars of additional services and equipment sales in this sector over the next few years.

Japan has also relaxed restrictions in its satellite services market, permitting a more than two-fold increase in the number of channels broadcasters can provide to Japanese consumers. Such measures will likely save service providers in this market millions of dollars, and permit them to offer the type of innovative, consumer-oriented packaging which is transforming the distribution of pay TV satellite services worldwide.

Building on these achievements, in this second year of the Enhanced Initiative, the United States is urging Japan to introduce LRIC as early as possible in the year 2000 to ensure that: (1) rates are market based; and that (2) before such a methodology is in place, Japan makes steady interim reductions towards this goal. The United States commends the Ministry of Posts and Telecommunications (MPT) for soliciting public comments on draft interconnection rate reforms. The United States further urges the MPT to act affirmatively and adopt the extensive, detailed comments it provided regarding ways to improve the interconnection regime in Japan.

Further, the United States believes Japan should, while liberalizing rules and requirements for non-dominant carriers, establish a system which imposes disciplines on dominant carriers, such as NTT and its wireless subsidiary NTT DoCoMo, which employ practices which distort competition. To this end, the United States is encouraging Japan to create a regulatory distinction between dominant carriers and new market entrants in its administration of: (1) approval of end-user rates, (2) approval of terms and conditions for new services, (3) rights-of-way, and (4) other areas where market power may impede competition.

Similarly, Japan's communications satellite services market continues to be plagued by outdated regulations, developed in the era of analog broadcast transmission, which are hampering the development of innovative service offerings made possible through new digital technologies. The United States proposes that this system be abolished for digital direct-to-home satellite providers, giving such providers freedom to provide innovative digital-based services.

Housing: Under the Enhanced Initiative, the United States and Japan established a Housing Experts Group which met in February and November of 1998. The group promotes improved market access in Japan for foreign suppliers of wood and building products consistent with the 1990 U.S.-Japan Wood Products agreement and focuses on full implementation of Japan's March 1996 Deregulation Action Program which envisages a one-third reduction in Japan's housing costs by the year 2000, and places a special emphasis on improved access for imported building products. Improved market access for wood and other building products and reliance on performance-based standards will lead not only to increased opportunities for American exporters, but also to higher quality, safer, and more affordable housing in Japan.

Our efforts on this front have led to several significant changes, including the development of a performance-based standard for 2x4 construction, as well as testing methods and procedures for implementation; recognition of U.S. grademarked-lumber for use in 2x4 construction in Japan; the lifting of the ban on construction of three-story, multi-family wood-frame housing; and reform of the Building Standards Law (BSL) to move from prescriptive to performance-based standards. Before the downturn in the housing market, U.S. industry had estimated that these changes could expand the market for U.S. wood products in Japan by $500 million annually by the end of the decade. Unfortunately, progress on implementation has been slow, but the United States will continue to closely monitor the sector to ensure that Japan abides by its commitments.

Another long-standing U.S. objective in Japan has been the elimination of tariffs on value-added wood products. At the November 1998 APEC Summit, APEC economies, including Japan, agreed to: (1) participate in WTO negotiations on the tariff elements of the nine sectoral initiatives developed by APEC , including forest products (which covers wood, paper, printed materials and wood furniture); and (2) seek conclusion of a WTO Agreement in 1999, which would lead to the phase-out of tariffs for wood products by 2004.

Financial Services: Japan's pool of individual and institutional savings -- valued at some $10 trillion -- is the largest outside the United States. The Japanese Government's proposed "Big Bang" liberalization of its financial services industry should substantially improve the ability of foreign financial services providers to reach customers in most segments of the Japanese financial system.

Among the more important measures being implemented under the "Big Bang" initiative are those related to liberalizing securities derivatives, easing the registration process for new securities companies, promoting a more vigorous asset-backed securities market, and significantly expanding the scope of financial services and products allowed to be offered by banks and securities firms, including investment trust (mutual fund) products. In addition, the notion of making stock options available has been introduced, and brokerage commissions are to be fully liberalized. The April 1 revision of the Foreign Exchange Law is also expected to ease capital flows and access to foreign exchange.

The United States welcomes Japan's successful implementation of the measures contained in the 1995 U.S.-Japan Agreement on Measures Regarding Financial Services, as well as Japan's actions taken to date under its "Big Bang" financial deregulation initiative. Further regulatory reform of Japan's financial markets will increase competition, help improve Japan's long-term growth prospects and contribute to a wider variety of investment opportunities for individuals and Japanese companies.

In this context, the United States has proposed that Japan adopt the following deregulatory measures at the earliest possible date: (1) favorably consider the adoption of a *tokkin* framework for the management of publicly-administered savings, including *Nempuku*, *Kampo* and *Yucho* funds; (2) eliminate the requirement that fund sponsors liquidate all investments when shifting business from one asset manager to another; (3) expand the scope of business opportunities for securities companies to offer new products and services; (4) eliminate restrictions on nonbanks' use of proceeds from bond and commercial paper issuance; (5) enhance disclosure by financial institutions (including fund managers) to market participants; and (6) introduce tax-advantaged defined contribution pension plans.

The United States is urging Japan to improve transparency in the financial services sector by: (1) establishing an open and transparent process for the approval of new products and services; and (2) instituting notice and comment procedures for all new regulations, thereby providing sufficient time between finalization of regulatory changes and implementation to allow industry a fair opportunity to undertake necessary organizational, operational and systems-related changes.

Medical Devices/Pharmaceutical Products: Japan's over-regulation of medical devices and pharmaceuticals has hindered the introduction of innovative, cost-effective American products into Japan's market, and prevented many Japanese patients from receiving the most advanced medical care available.

Under the Enhanced Initiative, by April 1, 2000, Japan is to cut the approval period for new drugs by one-third, from 18 months to 12 months. This measure will allow the introduction of new medicines in Japan on a more timely basis, which will benefit both Japanese consumers and U.S. manufacturers alike. American firms, which currently hold a 12-percent share of Japan's $60 billion pharmaceuticals market, stand to reap substantial benefits from a faster drug approval process. Japan has also committed to greatly expand the acceptance of foreign clinical data in its approval of new medical devices and pharmaceuticals, which promises to significantly reduce the time and expense U.S. firms must devote to new product testing and approvals. Since U.S. medical device firms currently sell over $5.5 billion of equipment in Japan's $20 billion medical device market each year, faster introduction of innovative products means increased access for American firms.

Further, as it formulates health care reforms, Japan has agreed to place a high priority on recognizing the value of innovative products. This action will facilitate the prompt introduction of innovative, cost-effective products for Japanese patients by U.S. firms, which lead this sector in cutting-edge technologies.

For 1999, the United States is urging Japan to adopt a market-based pricing system, to promote the introduction of innovative pharmaceuticals, and to work constructively with industry and interested parties to develop, as soon as possible, streamlined and transparent procedures for the prompt creation of new functional reimbursement categories for medical devices. With regard to the introduction of a reference pricing system for drugs, the United States remains strongly opposed. Reference pricing, in any form, by its structure and purpose, is not compatible with innovation and instituting such a system would certainly impede the introduction of innovative life-saving and cost-effective drugs in Japan.

The United States has put forward several specific proposals to speed the approval and reimbursement of innovative medical devices and pharmaceuticals.

For example, the United States calls on Japan to: (1) ensure that decisions made by reviewing personnel are binding on the reviewing institution, as well as others involved in the process; and (2) eliminate inconsistencies between reviewing bodies interpretations of the acceptability of foreign clinical data.

The United States also strongly urges Japan to make steady and continuous progress in shortening the approval processing period for new drug applications as Japan implements the measures in the Joint Status Report to approve new drug applications within 12 months by April 2000. U.S. proposals include: (1) allowing direct communications between applicants and reviewing committees; and (2) specifying clearly the criteria, the selection review process, and the time frame for approval of applications for priority product treatment.

Energy: Japan is beginning to deregulate its $150 billion energy sector with the aim of reducing energy costs, which are the highest in the industrialized world. Such deregulation will benefit the Japanese economy and improve foreign access to this market. In order to assist in this undertaking and to address specific regulatory issues of concern to U.S. firms in this sector, the United States and Japan established a new working group under the Enhanced Initiative, which held its first meeting in October 1998. During this meeting, the group discussed Japan's plans for partial liberalization of the electric utility sector. Specifically, the United States called on Japan to revise and streamline the testing, inspection, and information requirements under the High Pressure Gas and Electricity Utilities Industry Laws. The United States also requested that Japan: (1) review and streamline onerous national, prefectural, and local restrictions, particularly those which make updating of existing power generation facilities uneconomical; (2) accept foreign and international test data and product certifications for standby generator sets; (3) streamline the regulatory and approval process for self-service gasoline stations and pumps; (4) enhance transparency and strengthen its competition policy advocacy and enforcement efforts in this sector; and (5) accelerate privatization and reliance on voluntary, market-driven standards related to the energy sector.

Legal Services: As set out in the Joint Status Report, the Japanese Diet has enacted legislation that reduces restrictions on foreign lawyers in Japan. In particular, the new law reduces the length of experience required of foreign lawyers before they are allowed to register as foreign legal consultants (*gaikokuho-jimu-bengoshi*) in Japan (from five years to three years) and allows foreign lawyers to count the time they spent practicing their home country's law in a third country toward meeting the experience required to register as a *gaikokuho-jimu-bengoshi* in Japan. Further, Japan agreed to liberalize the ability of a *gaikokuho-jimu-bengoshi* to practice third country law in Japan, based upon written advice from a lawyer qualified in that third country.

Notwithstanding, Japan continues to maintain unreasonable and unnecessary restrictions on the provision of legal services which prevent both foreign and Japanese lawyers from offering clients fully integrated transnational legal services for domestic and cross-border transactions. The United States has requested that Japan: (1) remove the prohibition against partnerships between Japanese lawyers (*bengoshi*) and *gaikokuho-jimu-bengoshi* and the prohibition against the employment of *bengoshi* by *gaikokuho-jimu-bengoshi*; (2) allow a foreign lawyer to credit all of the time spent practicing the law of the lawyer's home jurisdiction in Japan toward meeting the experience required to register as a *gaikokuho-jimu-bengoshi*, rather than just the one year allowed under current practice; and (3) remove the partnership, employment and cost-sharing restrictions on relationships between quasi-legal professionals and *bengoshi* and *gaikokuho-jimu-bengoshi*.

Structural Deregulation

Distribution: The United States welcomed the passage in 1998 of legislation in Japan abolishing the Large Scale Retail Store Law, long identified as a significant impediment to the establishment, operation, and expansion of large retail stores. The United States believes that deregulation and the introduction of competition into Japan's retailing sector is long overdue. Japan's Ministry of International Trade and Industry (MITI) is in the process of implementing new legislation, the Large-Scale Retail Store Location Law, or *Daiten Ricchi Ho*, which transfers authority with respect to the establishment of large stores to local governments. The *Daiten Ricchi Ho* will restrict local governments' role in the establishment of large stores to considering environmental factors, such as traffic and noise.

The smooth transition to a new pro-competitive regime will continue to be an important issue for discussion under the Enhanced Initiative. In the October 1998 U.S. submission, the United States called on Japan to: (1) adopt guidelines for implementing the new Large-Scale Retail Store Location Law which precisely define the environmental criteria local governments will be allowed to consider; and (2) carefully and continuously monitor local governments' application of the law to ensure that it is being used to address legitimate environmental concerns only and is not being used to thwart competition. A study group responsible for drafting these guidelines is to be created and the United States urges MITI to make the operations of the study group open and transparent so as to incorporate the views of large retailers in its final report. The United States also urges MITI to establish a formal process for hearing and acting upon retailers' complaints where local governments unreasonably seek to restrict the establishment of large retail stores.

Competition Law and Policy: At Birmingham, Japan agreed to implement specific measures designed to promote competition within its markets. For example, the Japan Fair Trade Commission (JFTC), as part of its effort to more vigorously enforce its antitrust laws, agreed to survey Japan's top 2,000 firms to assess their Antimonopoly Law compliance programs. The JFTC also agreed to follow up on its industry surveys to ensure that firms take appropriate actions to correct practices about which the JFTC has raised concerns, particularly the film and glass sectors. In view of such concerns and in line with U.S. proposals, Japan: (1) established study groups to consider mechanisms designed to permit private parties to sue for injunctions against violations of the Antimonopoly Act; (2) agreed to submit legislation to the Diet abolishing certain exemptions to the Antimonopoly Act; and (3) agreed to undertake specific measures aimed at preventing bid-rigging.

The United States strongly believes that the JFTC should substantially boost its efforts as an advocate of competition policy and regulatory reform by championing the removal of competition-blunting regulations -- especially those regulations which block new firm entry. In 1999, the United States proposes that the JFTC establish a Competition Policy Bureau to act as an assertive competition advocate by promoting competition and regulatory reform in sectors of the Japanese economy that are, or may be, subject to government regulation. The United States also proposes that the JFTC introduce a Retail Sector Competition Promotion Initiative which will closely monitor the activities of those local and prefectural governments considering large-scale retail store establishment requests. Under this initiative, the JFTC would make submissions to these governments regarding the procompetitive effects of large-scale retail stores.

The United States also strongly believes that the genuine availability of injunctive relief and damages through private litigation is an integral part of a comprehensive antimonopoly legal regime. As such, we urge Japan to amend the Antimonopoly Law (AML) to lift legal restrictions on private injunctive relief and private damage actions for alleged AML violations. The United States also seeks further strengthening of criminal enforcement of the AML.

Transparency and Other Government Practices: Historically, Japanese regulations have been developed in a "black box", to which only insiders have had access. This issue is considered by the United States to be an important agenda item in continuing discussions under the Enhanced Initiative. At Birmingham, Japan agreed to implement measures designed to increase the transparency of, and reduce the burdens imposed by, its administrative system. To this end, Japan is undertaking implementation of proposed public notice and comment procedures for use when ministries and agencies develop regulations. The United States strongly urges Japan, specifically the Management and Coordination Agency, to address the serious deficiencies identified in the U.S. comments when it prepares the final version of Japanese Government-wide public comment procedures. The United States believes it is particularly important that Japan greatly reduce the broad discretionary powers given to ministries and agencies with regard to limiting the coverage and application of the public comment procedures.

The United States has also made several proposals to Japan aimed at rectifying the burdensome and unpredictable nature of Japan's approval process, in particular those processes used by the Ministry of Finance, the Financial Supervisory Agency, the Ministry of Construction, and the Japan Harbor Transport Association. Relative to this, Japan agreed at Birmingham to review the examination standards and to accelerate the issuance of approvals. Among U.S. proposals include those relating to concern that industry associations and other private sector organizations will be allowed to substitute private sector regulations (so-called "*min-min kisei*") in place of government regulations. In addition, the United States urges the Japanese Government to enact an Information Disclosure Law and to make its advisory council system more transparent by requiring the use of notice and comment procedures when these councils issue interim reports and preliminary recommendations. Further, the U.S. urges Japan to allow foreign non-governmental persons and foreign companies to participate either as members of, or as observers at, advisory council meetings.

Civil Aviation

In January 1998, the United States and Japan concluded the U.S.-Japan Civil Aviation Agreement. The agreement is intended to significantly liberalize the civil aviation market between Japan and the United States and is expected to result in substantial economic benefits for both U.S. carriers and passengers, with U.S. aviation service-related exports expected to increase by $1 billion annually. In addition, this agreement provides for further negotiations within three years aimed at establishing a fully liberalized bilateral aviation regime, with additional concrete liberalization measures to automatically come into force should such negotiations not be concluded by 2002.

This new Civil Aviation Agreement provides numerous concrete opportunities for both U.S. passenger and cargo carriers. For example, under this agreement the number of flights to Japan by current U.S. non-incumbent combination carriers (e.g., Delta, American and Continental) will increase significantly. In addition, two new U.S. non-incumbent combination carriers will also be provided with access to the Japanese market, while non-incumbent all-cargo carriers (e.g., United Parcel Service and Polar Air Cargo) will gain valuable new opportunities to transport cargo to destinations beyond Japan. This agreement also eliminates restrictions and resolves serious disputes for U.S. incumbent carriers. For example, the agreement lifts all restrictions on both the number of flights operated, and points served between the U.S. and Japan by incumbent combination and all-cargo carriers (e.g., United Airlines, Northwest Airlines and Federal Express) and should resolve the long-standing dispute over our incumbent carriers' rights to fly from Japan to other international points beyond Japan.

Further, for the first time, codesharing between U.S. and Japanese carriers, among U.S. carriers (on many operations), and between U.S. and third-country carriers, is permitted as a result of this agreement. In addition, charter operations are also increased. Finally, the agreement promotes competition by guaranteeing U.S. carriers fair and equal opportunity to contract with wholesalers and travel agents and to establish enterprises to market their services directly to consumers.

In general, implementation of the agreement proceeded smoothly over the balance of 1998. Unfortunately, recession in Japan and much of Asia has resulted in slower than expected expansion of U.S. aviation services in those markets. Nevertheless, U.S. carriers did take advantage of new rights provided for under the agreement. Specifically, new routes were opened, frequencies were added, and United Airlines formed a codesharing alliance with All Nippon Airways (ANA). Although disagreement over interpretation of third-country codeshare rights did cause a delay in the approval of the first codesharing application between a U.S. and third-country carrier to serve Japan, that disagreement appears to have been favorably resolved. We will continue to closely monitor that situation and will insist that Japan continue to consistently apply such third-country codesharing provisions. The United States is also closely monitoring the renovations at Tokyo's Narita Airport to ensure that the ability of U.S. carriers to serve that important market is not unduly impaired.

Existing Bilateral Agreements: Implementation and Monitoring

Insurance

The United States and Japan have concluded two bilateral agreements on insurance. The goal of the first, the 1994 U.S.-Japan Insurance Agreement, is to achieve a substantial increase in market access and sales for competitive foreign insurance providers and intermediaries in Japan. On December 15, 1996, the United States and Japan announced agreement on the second, a series of supplementary measures to the 1994 insurance agreement. These detailed measures are designed to ensure increased competition, allow greater product innovation and pricing flexibility, lower premiums for Japanese consumers, and increase market access for U.S. and other foreign insurance providers in Japan's insurance market. The focus of the supplementary measures is on the "primary sectors", which account for roughly 95 percent of Japan's insurance market.

Among other measures, Japan agreed to avoid radical change in the "third sector" for a "reasonable period" following substantial deregulation of the "primary" life and non-life sectors. The third sector, which includes personal accident, cancer, and hospitalization insurance, while only comprising five percent of Japan's overall insurance market is a segment of Japan's insurance market of particular importance to foreign insurance providers.

In general, Japan has made some progress in deregulating its insurance sector. In September 1997, Japan approved automobile insurance with rate differentiation and has also expanded product coverage under its notification system and lowered the threshold for rate flexibility in commercial fire insurance.

However, the United States remains concerned with Japan's inaction relative to the implementation of other insurance-related deregulatory measures. At consultations in June 1998, the United States noted its serious concern that, in particular, Japan has not fully implemented its obligations regarding reform of its rating organizations, which act as cartels imposing uniform industry-wide insurance rates on consumers for products such as voluntary automobile insurance and fire insurance. Japan also failed to fully implement its obligations to approve new product and rate applications within the standard 90-day processing period. Given that all of the primary sector deregulation criteria had yet to be fulfilled, USTR announced on July 1, 1998, that the United States does not support the initiation of the two-and-one-half year clock to open the third sector of Japan's insurance market, as anticipated under the 1996 Agreement. In addition, the United States is thus seriously troubled by the apparent diminution of the third sector safeguards caused by increased activity on the part of Japanese insurance firms and subsidiaries in this segment of the market. For example, the United States is extremely concerned with Japan's licensing of a cancer rider to Tokyo Anshin, the life subsidiary of a large Japanese insurance company, Tokyo Fire and Marine.

The United States seeks to address our outstanding differences with Japan on insurance through a constructive engagement. Furthermore, the United States expects Japan to fully adhere to its clear obligation under these agreements to consult with the United States upon request.

Flat Glass

In January 1995, the United States and Japan concluded an agreement (Flat Glass Agreement) aimed at opening the Japanese market to imported flat glass. Japan's $4.5 billion flat glass market had been dominated by an oligopoly of three large producers, each with separate and exclusive distribution systems, since the late 1960's. In coordination, these producers changed prices, capacity, and product mix in virtual lockstep, thereby maintaining constant market shares.

The Flat Glass Agreement recognizes that Japanese glass firms will take a variety of measures to assure that foreign glass has full access to Japan's distribution network. The Government of Japan also commits in the Agreement to remove discrimination in public works projects, to promote the use of insulated and safety glass (types of glass of which U.S. companies lead in low cost and high quality), and to conduct an annual survey to assess the openness of the distribution network.

The agreement has helped American firms, but only to a certain extent. For example, it did induce Japan to feature American glass in a number of high-profile public construction projects. In addition, it obligated Japan to adopt new energy conservation standards that will raise the demand for insulated glass. But the basic problem remains the same: U.S. and other foreign suppliers enjoy only token access to the distribution network controlled by the three major Japanese glass manufacturers. As a result, in spite of the dedicated efforts of U.S. glass manufacturers, the high quality of their products, and competitive pricing, their small market share has barely changed since the Agreement was signed.

Concerns about inadequate progress prompted the United States in the spring of 1998 to seek: (1) an update of the 1993 JFTC survey of the flat glass industry; and (2) Japanese Government participation in an initiative to strengthen antitrust compliance in Japan. Japan accepted the first proposal, and the survey is now underway, with completion expected by spring 1999. Japan rejected the compliance initiative, prompting the United States to provide the JFTC and MITI with an in-depth analysis of the flaws in the antitrust compliance plans of two Japanese flat glass manufacturers. In response, Japan indicated that the JFTC's upcoming survey of the sector would examine this issue.

The United States and Japan will hold the next annual consultation under the Flat Glass Agreement in the Spring of 1999, at which time another MITI survey covering the fourth year of performance under the Agreement will be reviewed.

Government Procurement

Overview: Over the last decade, the United States and Japan have implemented eight bilateral Government Procurement Agreements covering the areas of: telecommunications (including an agreement covering Nippon Telegraph and Telephone (NTT) procurement), computers, supercomputers, satellites, medical technology, and construction/public works. The overall goal of these agreements is to expand Japanese public procurement of competitive foreign products and services by addressing traditional Japanese procurement practices which have historically prevented U.S. and other foreign firms from fully and equally participating in the Japanese public market. These agreements address, for example, the lack of consistent and equal access to information regarding upcoming procurements; the insufficient opportunities to comment on, and participate in, the development of specifications; Japan's over-reliance on sole-sourced procurements; and the lack of impartial bid protest systems.

Despite some meaningful progress under the Medical Technology, NTT, and Satellite Agreements, results to date under many of the bilateral government procurement agreements have been disappointing. The United States is seriously concerned that, overall, the goals of these agreements are not being fulfilled, noting, for example, that there continue to be significant disparities between the foreign presence in the Japanese private and public sectors in many sectors covered by these agreements. Japan's recent plans to focus significant supplemental budgetary spending on new high-tech projects designed to lead Japan into the 21st Century make full implementation of fair, open, and transparent procurement procedures all the more important.

Telecommunications Government Procurement: The Government Procurement Agreement on Telecommunications Products and Services, concluded on October 1, 1994, aims to significantly increase access for, and sales of, foreign competitive products and services. The agreement also includes measures Japan will take to improve and open its procurement process to foreign suppliers and which are intended to improve the transparency and impartiality of the process and to increase reliance on international standards. Implementation of this agreement is assessed through both quantitative and qualitative criteria.

The United States is disappointed with the results of this agreement as assessed at the most recent annual bilateral review held in February 1998. While the share of foreign telecommunications imports of the Japanese Government procurement market (by value) increased from 7 percent in 1994 to 13 percent in 1995, this share declined to a mere 3.5 percent in 1996. Preliminary 1997 figures (provided by Japan) show that foreign market share continues to remain at an unacceptably low level. While the cause of this poor performance is not yet fully clear, initial indications are that Japanese Government practices continue to diminish the attractiveness of its government procurement market. This is particularly evident when compared with Japan's private sector market where opportunities are greater and where foreign firms have registered substantial gains. The United States is seriously concerned with this downward trend in Japanese public procurement of world-class foreign goods and services and will continue to vigorously pursue this issue with Japan. The next annual review is scheduled for the spring of 1999.

NTT Procurement: Nippon Telegraph and Telephone (NTT) is Japan's largest user of telecommunications equipment and services, with NTT contracts alone representing more than a 1 trillion yen procurement market in 1997. Inadequate coverage of NTT equipment purchases under the General Agreement of Tariffs and Trade (GATT) Government Procurement Code led the United States to sign a separate NTT agreement in 1980. On September 30, 1997, the United States and Japan concluded a new agreement extending and improving the 1980 NTT Agreement. Under this agreement, NTT and the Government of Japan committed to: (1) provide greater access to technical information necessary to build equipment for NTT's network; (2) provide more information to suppliers regarding NTT's procurement plans for key equipment; (3) extend coverage of the agreement to NTT's new software subsidiary; (4) reduce the number of unique standards used by NTT which disadvantage foreign suppliers; and (5) apply principles of openness and non-discrimination to NTT's procurement practices. Several NTT subsidiaries are now covered under the agreement, including NTT Mobile Communications Network, Inc., NTT Power and Building Facilities, Inc., and NTT Communications Corporation Inc. This is the sixth time since 1980 that the NTT Agreement has been renewed, and it will continue in force until NTT is restructured in 1999.

The last annual review of the NTT Agreement was held in Tokyo in October 1998. At that time, the United States was encouraged by the 1997 data presented by Japan which showed, overall, a notable increase in NTT procurement of foreign telecommunications equipment over the previous year, bringing 1997 foreign sales to NTT to 185 billion yen. Despite this progress, however, results to date under the NTT Agreement still fail to match the success foreign firms have achieved in other, more open parts of the Japanese market and telecommunications markets globally. Accordingly, the United States expects continued growth in NTT's procurement of foreign equipment.

Computers: The January 1992 U.S.-Japan Government Procurement of Computers Agreement commits Japan to adopt non-discriminatory and open procurement procedures with the aim of expanding government procurements of foreign computer products and services. The agreement makes procedural improvements in Japan's public sector computer procurement regime, with provisions guaranteeing that: (1) equal access to information and opportunity to participate will be available to all potential bidders; (2) any company that has participated in developing specifications for a procurement will be barred from bidding on that same procurement; (3) sole sourcing will be restricted to exceptional cases justified under the GATT/WTO code; (4) evaluation of bids will be based upon a range of criteria set forth in the tender documentation; and (5) unfair low bids will be prohibited.

At the August 1998 annual review of the agreement, the United States expressed serious concern over the 37 percent plunge in Japanese public procurement of foreign computers goods and services between FY95 and FY96, as disclosed by data provided by the Japanese Government. The United States also expressed concern that U.S. industry data for FY96 shows a disturbing 50 percent decline in foreign share of the Japanese public sector personal computer market since the agreement was implemented in 1992. Further, this data indicates that there has also been a two-year decline in Japanese public procurement of foreign mid-range/mainframes, evidencing a disturbing overall downward trend in this sector. This is particularly disappointing in view of the fact that the foreign (principally U.S.) firms have maintained more than a 30 percent share of the competitive Japanese private sector computer market.

In light of this situation and taking into account technological advancements in this sector, the United States presented Japan with a series of proposals for updating and improving the implementation of the agreement at the August 1988 review. These proposals, which are consistent with what Japan has already committed to under the 1994 Telecommunications and Medical Technology Agreements, center on the broader adoption in Japan of the "overall greatest value methodology", as well as provision of advance information to potential bidders on a larger number of upcoming procurements. These proposals are still under discussion.

Satellites: The U.S.-Japan Satellite Procurement Agreement obliges Japan to implement open, transparent and non-discriminatory procurement procedures, thereby opening up non-R&D satellite procurements, including those conducted by Nippon Telegraph and Telephone (NTT) and Nippon Hoso Kyokai (NHK), to foreign satellite makers. To date, the Agreement has been successfully implemented with U.S. firms winning all of the procurements covered by the agreement. The United States continues to monitor Japan's adherence to the terms of the agreement, especially in light of recent Japanese Government announcements related to satellite programs.

Supercomputers: Under the 1990 Supercomputer Agreement, Japan committed to implement transparent, open and non-discriminatory procurement procedures and to ensure that procuring entities are able to procure the supercomputer that best enables them to perform their missions.

Results under the 1990 Supercomputer Agreement have, generally, not been satisfactory, and a significant gap still exists between the U.S. share of the competitive Japanese private sector and the Japanese public sector supercomputer markets. Although there was a notable increase in the U.S. share of Japanese public sector supercomputer market in FY93 and FY94, during which time U.S. firms obtained a 40-45 percent market share, this positive trend has been reversed in recent years. U.S. firms won only one of eleven procurements in FY95, two of eight procurements in FY96, and only one of five supercomputer procurements in FY97.

During the August 1998 consultations, the United States raised concerns over Japan's implementation of the agreement, specifically as it relates to the use of inappropriate technical requirements in public supercomputer procurements. These requirements appear to have been drafted in a way as to exploit design differences between what may otherwise be equally qualified U.S. and Japanese systems, in favor of Japanese vendors. The United States will continue to press Japan to ensure that the terms of the Supercomputer Agreement are faithfully implemented, including the use of neutral and non-discriminatory technical requirements.

The United States and Japan also agreed at the August 1998 consultations to open discussions on revising the threshold for coverage under the agreement, based on advances in computing technology since coverage was last revised in 1995.

Medical Technology: The Medical Technology Agreement was concluded in November 1994 with the goal of significantly increasing access and sales of competitive foreign medical technology products and services in the Japanese public sector procurement market.

The most recent annual review of the agreement was held in June 1998, at which time Japan presented data for FY96 which showed a modest 3.2 percent increase in the foreign share of the market over the previous year. Preliminary FY97 figures indicate that foreign market share increased slightly again between FY96 and FY97. The United States has noted that the Medical Technology Agreement is currently one of the few bilateral government procurement agreements in which consistent positive growth trends are evident.

As a result, the United States is satisfied that Japan is demonstrating a general adherence to the intent of the arrangement to provide greater market access and sales in Japan's government procurement sector. However, the United States continues to press for strict compliance with the agreement's provisions, greater transparency in Japan's public procurement process, and the expanded use of overall greatest value methodology to include procurements by local and prefectural governments.

Construction/Public Works: There are currently two construction/public works agreements in effect: the Major Projects Arrangement (MPA), implemented in 1988 and amended in 1991, and the 1994 U.S.-Japan Public Works Agreement, which includes the "Action Plan on Reform of the Bidding and Contracting Procedures for Public Works" (Action Plan). The MPA was designed to improve access to Japan's public works' construction market and includes a list of 40 projects in which international cooperation is encouraged. Under the Action Plan, Japan must use open and competitive procedures on procurements valued at or above the thresholds established in the WTO Government Procurement Agreement.

During the June 1998 review of the 1991 and 1994 agreements, the United States was disappointed to learn that U.S. firms had won only $50 million in public works contracts. This fell far short of the $100 million won by U.S. firms in public works contracts the previous year and the $300 million in contracts won during the peak year in 1989. The U.S. share of Japan's $250 billion public works market has consistently remained under 1 percent – a troubling fact given the competitiveness of U.S. firms throughout the rest of the world.

Because of the discouraging results reported in the 1998 annual review, the United States requested special interim consultations on the agreements which are to be held in January 1999.

Autos and Auto Parts: The chronic bilateral trade imbalance in the automotive sector continues to plague the U.S.-Japan relationship. The Administration committed to take the necessary steps to obtain a meaningful market access agreement that would result in significant opportunities in the Japanese market for competitive U.S. auto and auto parts manufacturers. In August 1995, the United States and Japan reached an Automotive Agreement with the objectives of eliminating market access barriers and significantly expanding sales opportunities in this sector. To monitor implementation of the Automotive Agreement, the United States also announced the establishment of an Interagency Enforcement Team, which publicly releases a semi-annual assessment of progress in all areas covered by the Automotive Agreement.

The latest monitoring report, issued on August 12, 1998, recognized the difficulties encountered by both domestic and foreign sellers in Japan caused by Japan's current recession. Nonetheless, it noted that U.S. market access concerns in this sector continue. In the Japanese automotive sector, domestic vehicle sales have fallen for 23 months as of December 1998. Foreign automakers have been disproportionately affected by the recent trends in this sector. Sales of motor vehicles produced by the Big Three in North America fell 34.5 percent in 1998, more than double the contraction of the Japanese auto market as a whole.

Japan's recession has compounded the difficulties faced by U.S. automakers in adding new, high-quality dealerships. An additional complicating factor has been a continued reluctance on the part of many Japanese dealers to carry foreign vehicles for fear of damaging their long-term relationships with Japanese automakers. The Big Three have added 192 new franchise agreements with Japanese dealers since the signing of the Agreement. In response to U.S. Government requests, while Japan has taken steps to ensure that dealers understand that they are free to carry the products of competing manufacturers, improving the competitive environment to some degree, further significant efforts are needed.

Further, the pace of deregulation in the auto parts aftermarket continues to be slow. In February 1998, Japan held public hearings on the U.S. proposal to revise regulations regarding the certification of mechanics employed by the new specialized garages, which were created under the Agreement. The proposal is intended to lower the labor costs of these garages thereby increasing their competitiveness and encouraging their growth. Based on the hearing, the Japanese Government plans to add/revise the regulations to allow for another category of mechanic certification.

Japan's recession, and the resulting loss of momentum for meaningful deregulation in the auto parts sector, have also hurt U.S. firms. Auto parts exports declined 7 percent in 1998, the first drop since the Agreement was signed. Although Japanese automakers continue to invest in production facilities in the United States, U.S. imports of auto parts from Japan were flat in 1998, after having declined in each of the previous two years following the conclusion of the Agreement.

To generate further progress under the Automotive Agreement, the United States offered 11 detailed proposals to Japan during the annual review of the Agreement, held in October 1998. Among these proposals were: (1) streamlining new vehicle registration procedures; (2) tailoring Japanese Government financial incentives so they can be more effectively used by interested automotive companies; (3) streamlining of the *shaken* inspection and repair requirements; (4) revising requirements for mechanics working in special certified garages; and (5) eliminating additional items from the disassembly repair regulations. The U.S. Government is holding detailed discussions with the Japanese Government relative to these proposals.

Investment: In July, 1995, the United States and Japan concluded the U.S.-Japan Investment Agreement (Investment Agreement) with the objective of increasing the traditionally low level of foreign direct investment (FDI) in Japan. Persistently low levels of FDI evidence the complex web of structural and regulatory barriers which, along with corporate and private resistance to mergers and acquisitions, present formidable barriers to foreign firms wishing to access Japan's economy. This agreement, recognizing that addressing investment will create new business opportunities for U.S. and other foreign firms, focuses on both structural change and strong government facilitation to attract much needed foreign investment into the Japanese economy. Within the agreement, Japan committed to: (1) promote investment; (2) implement better tax incentives and financing; (3) improve conditions for foreign participation in mergers and acquisitions; (4) reduce regulatory restrictions on foreign investment; and (5) facilitate efforts by foreign firms to build business ties with Japanese firms. Regrettably, however, implementation by Japan of these measures was either administered on an "ad hoc" basis or targeted at sectors of the Japanese economy where there is little incentive for U.S. firms to invest.

As such, in 1998, the United States and Japan took a number of steps to enhance facilitation and increase investment incentives. Japan adopted or proposed changes to its financial regulations and disclosure requirements, corporate tax code, employment services industry policies, and land policy guidelines which are designed to gradually improve conditions for mergers and acquisitions and new investment in Japan. And, while local governments in Japan continue to take an increased interest in investment promotion to the satisfaction of the United States, it is apparent that more needs to be done in order for such incentives to be effective.

Talks in July 1998 focused on improving the climate for Mergers and Acquisitions (M&A) with capital, land, and labor experts discussing how Japan's accounting systems, disclosure methods, and corporate governance--as well as its tax, employment, and land policies restrict the benefits of M&A and new investment activity. The U.S. noted that although the number and value of M&A transactions in Japan did increase fairly dramatically in 1998, they remain the lowest in the OECD and total foreign direct investment in Japan is still less that one percent of GDP. In October 1998, the United States presented Japan with 18 proposals aimed at improving the investment environment in Japan including recommendations relating to accounting reform, land reform, labor and employment agency reform, and pension reform.

While both governments agreed to produce a joint report which would recommend ways to improve Japan's investment environment and attract more foreign investment, as well as review the accomplishments and shortcomings of the Agreement, the United States remains concerned by both the lack of significant progress to date in implementing changes, and the refusal of Japanese Government officials to seriously discuss crucial structural reforms necessary to redress impediments to FDI. The United States will continue to work with Japan to remove structural and regulatory barriers, improve the investment climate, and increase the level of foreign direct investment in Japan.

Semiconductors: The United States and Japan concluded a second bilateral semiconductor agreement which came into effect on August 2, 1996, replacing the 1991 U.S.-Japan Semiconductor Agreement (Semiconductor Agreement). The new agreement encourages progress in market access and industry cooperation and will help to solidify the gains of recent years.

The 1996 Semiconductor Agreement contains within it an industry-to-industry agreement which requires cooperation among manufacturers in making available quarterly market reports and analyses. Under the agreement, the United States and Japan are to review such reports and monitor market access in the Japanese and other major markets. Both the government and industry agreements provide for participation by other interested governments and industries which have eliminated semiconductor tariffs or committed to eliminate such tariffs expeditiously. The agreement also sets up a Global Governmental Forum (GGF) in which governments and authorities of important semiconductor producing countries/economies meet annually to discuss semiconductor policy issues.

In April 1997, the EU and Korea agreed to eliminate their semiconductor tariffs by 1999 and were invited to participate in the industry-to-industry agreement and government consultations. One meeting of each of these bodies was held in 1998. Taiwan, which was invited to join the second annual meeting of the GGF in January 1998, will participate in the industry-to-industry agreement and in the government consultations in 1999. At the 1998 meeting, the governments received and reviewed reports from the industries relative to market size, market growth, and market shares of foreign semiconductor products in World Semiconductor Council member markets and other major semiconductor markets. Cooperative activities conducted under the industry-to-industry agreement were also reviewed. The governments also discussed market trends and developments, including those related to competitiveness and foreign participation, in major markets, and government policies and activities affecting the semiconductor industries.

During 1998, the U.S. Government announced a 33.3 percent average annual foreign share for 1997, and foreign shares of 31.7 percent in the first quarter of 1998 and 33.9 percent in the second quarter of 1998, the latest quarter for which data is available.

Sectoral Issues

Steel

The U.S. steel industry endured tremendous hardship in 1998 as a sudden and substantial drop in demand for steel in Japan and the rest of Asia created a huge oversupply, which Japanese companies diverted to the U.S. market. In 1998, steel imports from Japan surged 163 percent and accounted for 41 percent of the overall U.S. steel import growth. This resulted in Japan becoming the single largest exporter of steel to the United States, accounting for sixteen percent of all U.S. steel imports. Aggravating this situation was the fact that the vast majority of such exports involved high-quality steel which sold for artificially low prices.

On September 30, 1998, U.S. steel producers and workers requested a Department of Commerce dumping investigation concerning imports of carbon hot rolled sheet products from Japan. That investigation, which is ongoing, has since been expedited, consistent with regulatory guidelines. The Department of Commerce has also made a "critical circumstances" finding in this investigation with respect to steel imports from Japan which will ensure that any dumping margins found will be applied retroactively, again, consistent with U.S. law and international agreements.

Although December 1998 imports of steel from Japan declined from the extremely high levels of earlier months, 80 percent of the decline was accounted for by "hot rolled sheet" and "plate in coils" steel products, which are subject to the ongoing dumping investigation. On January 7, 1999, President Clinton sent a report to the Congress, stating, among other things, his expectation that Japan's exports will return to appropriate pre-crisis levels in 1999. The Administration has since announced its intent to monitor steel imports from Japan on a monthly basis, and stated that it stands ready, if necessary, to self-initiate trade actions under U.S. safeguards and antidumping laws, in order to ensure that steel imports from Japan are rolled back. The Administration informed the Government of Japan that additional and sustained reductions are needed to meet the President's expectation that imports promptly revert to the pre-crisis levels. Implementation of this, and other Administration steel trade initiatives, will remain a high priority for the 1999 trade agenda.

Rice: Japan's highly protected rice market has long been a target for liberalization efforts. During the GATT Uruguay Round (UR), Japan agreed to begin opening its domestic rice market and establish a minimum access commitment for rice imports. Under this agreement, Japan committed to import 379,000 metric tons in 1995/1996. This quota was to grow to just over 758,000 tons at the end of the Uruguay Round implementation period (2000/2001). Since the Uruguay Round, the United States has been the single largest foreign supplier of rice to the Japanese market, supplying approximately one-half of Japan's total imports.

In December 1998, Japan notified the WTO of its intention to convert Japan's current minimum access commitment for imported rice to a tariff rate quota (TRQ). The shift to a TRQ, which is provided for in annex 5 to the Uruguay Round's Agriculture Agreement, would replace the current absolute quota. By switching to a TRQ, Japan will be allowed to slow the rate of growth of the minimum access commitment in the final two years of the UR implementation period. This will result in a decrease of the minimum access commitment in 2000/2001 of about 76,000 tons of rice. The United States has expressed serious concern that Japan's actions run contrary to the liberalizing spirit of the Uruguay Round. We also raised concerns with respect to the methodology Japan used to calculate the tariff rates. To maximize the new over-quota tariff rate, Japan compared past prices of high-cost, high-quality domestic rice with the price of low-quality imported rice for manufacturing use. This methodology raises questions with respect to WTO consistency. Further, we expressed concern about the rapid pace in which Japan adopted this scheme, leaving no time for bilateral discussions in advance of the policy change.

The United States has shared these concerns with Japan on several occasions, and in 1999 will continue to press Japan to ensure continual market access in this sector, consistent with Japan's WTO obligations.

Multilateral/WTO Disputes and Settlements

Distilled Spirits: On December 15, 1997, the United States and Japan reached settlement of the WTO Dispute Settlement case brought by the U.S. against Japan's discriminatory liquor tax system. Under this settlement, Japan agreed to adjust its excise tax rates on several categories of distilled spirits in order to come into compliance with WTO rulings for whisky and *shochu* "A" by May 1, 1998, and for *shochu* "B" by October 1, 2000. Moreover, Japan has agreed to eliminate tariffs on all brown spirits (including whisky and brandy) and vodka, rum, liqueurs, and gin by April 1, 2002. These tariff cuts go well beyond those committed to in the Uruguay Round, when Japan deferred to 2004 its elimination of tariffs on brown spirits, and blocked tariff elimination on white spirits.

Key elements of the distilled spirits settlement include:

(1) effective May 1, 1998, the tax rate for whisky/brandy will be lowered to a rate of ¥10,225/kl, while the tax rates on *shochu* type A, liqueurs and "spirits" will be raised to the level of the current tax rate on vodka (¥9924/kl);

(2) effective October 1, 1998, the tax rate on *shochu* B will be raised to ¥7976/kl; and

(3) effective October 1, 2000, the tax rate on *shochu* B will be aligned with tax rates for all other types of white spirits at ¥9924/kl.

As a result of the significant reduction in taxes under this settlement, total exports of U.S. spirits to Japan in 1998 increased by 23% over 1997 and grew faster than exports to other markets, in spite of Japan's accession.. Of particular note, U.S. exports of bourbon to Japan were up 34 percent over this period. The United States will continue to closely monitor Japan's implementation of this settlement to ensure that, among other things, tax and tariff reductions are eliminated in accordance with the agreed upon schedule.

Consumer Photographic Film and Paper: On February 3, 1998, the Administration established an interagency monitoring and enforcement committee to review implementation of formal representations made by Japan to the WTO regarding its efforts to ensure the openness of its market to imports of photographic film and paper. The monitoring and enforcement committee surveyed the Japanese photographic film and paper market and assessed information and data obtained from U.S. and foreign film manufacturers and the Japanese Government. The committee issued its first semi-annual monitoring report in August 1998.

With regard to the availability of foreign film in the two main segments of the market, the report showed distinctly different trends. In the traditional photospecialty stores, which comprise nearly half of the Japanese film market by sales volume, competition continues to be less robust and availability declined slightly. Meanwhile, in "non-traditional" outlets, such as supermarkets, department stores, convenience stores, and other non-photospecialty stores, which comprise a segment of the market that is relatively more open and where competition is more vigorous than in the rest of the photographic materials market, the report found that the availability of foreign film has doubled over the past three years.

The report attributed the improved access in non-traditional stores to several factors. Among these are the heightened focus on this issue over the past few years as a result of U.S. trade actions, nascent structural changes in Japan's distribution system, and initial steps taken by Japan to address exclusionary business practices in this sector. Continued efforts by Kodak and other foreign film manufacturers to actively market their products in Japan also have played a role. Regrettably, however, the continued use by Fuji and its primary wholesalers of unreasonable business practices that exclude its competitors has contributed to the lack of improvement in access to the traditional photospecialty stores, which remain a key film distribution channel.

The report also cited specific areas where additional action by MITI and the Japan Fair Trade Commission (JFTC) is warranted. Among these are measures designed to: (1) improve dissemination of MITI guidelines regarding business and distribution practices; (2) ensure that new measures regulating large stores are not allowed to unreasonably restrict competition or to favor small-and medium-sized stores; and (3) intensify JFTC monitoring of Fuji actions, especially tying arrangements and retaliatory threats by Fuji against retailers who promote foreign brands or photographic film or paper.

In preparation for its next semi-annual film monitoring report, the monitoring and enforcement committee continues to closely scrutinize foreign access to this sector and the Japanese Government's efforts to open this market in accordance with its WTO representations. The committee will release its next semi-annual film monitoring report in spring 1999.

Varietal Testing of Fruits: In October 1997, the United States invoked dispute settlement procedures against Japan's requirement that established quarantine treatments be retested each time an additional variety of an approved product is presented for export from the United States. The United States challenged these requirements as inconsistent with Japan's obligations under the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (the "SPS Agreement").

On October 27, 1998, a WTO dispute panel ruled in favor of the United States. The Panel's main findings were that Japan's varietal testing requirement is maintained without sufficient scientific evidence, in violation of Article 2.2 of the SPS Agreement, and is inconsistent with Japan's transparency obligations under Article 7 and paragraph 1 of Annex B, since Japan has not published its testing requirements. The Panel limited its Article 2.2 finding to apples, cherries, nectarines and walnuts. Both parties appealed, and on February 22, 1999, the WTO Appellate upheld the Panel's main findings. The Appellate Body also expanded the product coverage of the decision to include apricots, plums, pears and quinces by finding that Japan had not based its testing requirement on a risk assessment, in violation of Article 5.1 of the SPS Agreement.

In addition to the WTO case, the United States is extremely concerned with Japan's failure to approve importation of five apple varieties and two cherry varieties. Although the effectiveness of quarantine treatments has never been shown to vary among varieties of the same commodity, Japan requires separate efficacy testing of certain quarantine treatments for pests for each variety of a fruit to be imported. This redundant requirement has no scientific basis and, because it imposes expensive and time-consuming testing on American producers, serves as a significant barrier to market access. Furthermore, Japan has failed to approve entry of the apple and cherry varieties despite recent U.S. Government testing that demonstrated the effectiveness of quarantine methods used by American producers for each variety. The United

States pressed these concerns at senior levels in 1998, and will continue to do so in 1999. Japan's failure to approve these varieties by April 1, 1999 will have a serious negative economic impact on U.S. agriculture producers as this would preclude U.S. industry from shipping its 1999 crop to Japan.

Western Europe and the Mediterranean

Overview

Created in 1957, the European Union (EU) has grown from six to fifteen member states, with Austria, Finland, and Sweden becoming the newest EU members states on January 1, 1995. The EU comprises a market of some 370 million consumers with a total gross domestic product (GDP) of over $8 trillion.

The EU in 1997 intensified its efforts to deepen the integration of its member states. On the trade front, the EU has largely implemented its Single Market or ("EC-92") program to dismantle barriers to trade and investment among its member states. The pace of additional integrative efforts over the next few years will be set by implementation timetables established by the Maastricht Treaty (affecting a wide range of areas including monetary, social, and foreign policy), which went into force on November 1, 1993, and amendments to Maastricht which emerged from the 1997 Intergovernmental Conference (IGC) - the so-called Amsterdam Treaty. Under the Maastricht Treaty schedule, eleven member states on January 1, 1999 launched in earnest the Economic and Monetary Union (EMU) program, the most prominent feature of which is the introduction of the new European single currency (the "euro"), set to replace national currencies by 2002.

The other major trade group within Europe has been the European Free Trade Association (EFTA), which through 1994 included Austria, Finland, Iceland, Liechtenstein, Norway, Sweden, and Switzerland (Austria, Finland, and Sweden, however, ceased EFTA membership upon their accession to the EU in January 1995). Formed in 1960, EFTA provides for the elimination of tariffs on manufactured goods and select agricultural products that originate in, and are traded among, its member states. The United States has generally enjoyed good trade relations with the EFTA countries.

In late 1991, the EFTA countries and the EU reached agreement on the formation of a European Economic Area (EEA), designed to strengthen significantly the free trade agreement already in place between the two groups. Switzerland rejected the EEA in a referendum at the end of 1992 and turned to negotiating a number of bilateral sectoral agreements with the EU on trade issues. The EU and the remaining EFTA states renegotiated elements of the EEA agreement so that they could proceed without Switzerland. A revised text of the EEA entered into force on January 1, 1994. In practice, the EEA involves adoption by the EFTA countries of approximately 70 percent of EU legislation and has been seen by a number of the EFTA countries as a stepping stone to full membership in the EU.

Both the EU and EFTA have been negotiating free trade agreements with many of the countries of Central and Eastern Europe and the Mediterranean. The EU has signed association agreements and other types of free trade arrangements with the Czech Republic, Slovakia, Hungary, Poland, Bulgaria, Romania, Latvia, Lithuania, Estonia, Albania, Slovenia, Israel, Algeria, Morocco, and Tunisia. Each of the agreements are in force except for the agreements with Tunisia, Morocco, and Algeria. It is not clear when those agreements will be ratified. The EU has also negotiated a customs union with Turkey. Among other things, these arrangements provide for phased-in free trade in a number of sectors, notably excluding much or all of the agricultural sector, between the respective countries and the EU. EFTA has negotiated free trade agreements with Romania, Hungary, Bulgaria, the Czech Republic, Slovakia, Turkey, Israel, Poland, Slovenia, and Albania.

In December 1997, the EU at its Luxembourg summit decided to invite several Central and Eastern European countries (plus Cyprus) to begin a pre-accession process aimed at bringing them into the EU. Central and Eastern European countries in the group include Poland, the Czech Republic, Hungary, Slovenia, and Estonia. This pre-accession process began in March 1998, with an intensive "screening" of domestic legislation in these candidate countries for conformity with EU law. Subsequently, the EU formally launched substantive accession negotiations with these six "first-tier" candidates in November 1998. No firm target has been set for completing the negotiations, but some candidate states have expressed concern that the process could drag out for a number of years. Additionally, Bulgaria, Latvia, Lithuania, Romania and Slovakia have also applied for EU membership and may be invited to begin accession negotiations in coming years. In order to accommodate the eventual entry of the candidate countries, the European Commission has proposed reform of key Community institutions, as well as economic policies such as the Common Agricultural Policy and structural assistance funds for lower income member states.

Mediterranean

The U.S.-Israel Free Trade Area Agreement has been in force since 1985. This agreement is the only bilateral free trade agreement outside North America that the United States has entered into to date. The agreement has helped to expand two-way trade by phasing out tariffs and by reducing nontariff barriers to trade. All tariffs on industrial goods were eliminated as of January 1, 1995.

On December 4, 1996, the United States and Israel signed the Agreement on Trade in Agricultural Products. This agreement provides for improved market access for priority U.S. agricultural commodities on an immediate basis and to ensure steady market for the future.

On September 1, 1998, an agreement was published on market-opening measures, exempting Israeli products from customs user fees and adding Israel to the list of Eligible Countries under the Rural Electrification Act, in return for reciprocal concessions. Those concessions included: the elimination of metric packaging requirements and adoption of unit pricing procedures for domestic retail sales; an increase in the tariff rate quota for U.S. in-shell almonds; and a number of steps to facilitate the importation of U.S.-manufactured automobiles.

The United States has some continuing concerns regarding access to the Israeli market, which are being addressed within the framework of the Agreement. Israel's ban on the importation of non-kosher beef is of particular concern.

Intellectual property rights protection remains a top Administration priority in the Mediterranean region. Because of the Israeli Government's repeated failure to make good on promised legislative reforms and the absence of serious attempts by Israel to rein in piracy of intellectual property, on May 1, 1998, Israel was elevated to the "Special 301 Priority Watch List." Egypt, Turkey, and Greece also are on the Priority Watch List; while Jordan, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE are on the Watch List.

On March 6, 1998, Ambassador Barshefsky designated an industrial park in the city of Irbid, Jordan as the first "Qualifying Industrial Zone" (QIZ) from which goods can enter the United States duty-free. This action was pursuant to legislation passed by the Congress in October 1996, authorizing the President to proclaim elimination of duties on articles produced in the

West Bank, Gaza Strip and qualifying industrial zones in Israel and Jordan and Israel and Egypt. President Clinton issued a November 1996 proclamation delegating the authority to designate qualifying industrial zones to the U.S. Trade Representative and providing duty-free treatment to products of the West Bank and Gaza.

Negotiations with Saudi Arabia, Oman and Jordan on their accession to the WTO continue. In all three accession negotiations, the Administration continues to insist on entry based on implementation of WTO provisions upon accession and commercially meaningful market access commitments for U.S. goods, services and agricultural products.

European Union

Transatlantic Economic Partnership

At the May 18 U.S.-EU Summit in London, President Clinton and EU Leaders announced the Transatlantic Economic Partnership (TEP) initiative, which seeks to deepen and systematize the cooperation in the trade field launched under the New Transatlantic Agenda process begun in 1995 (See below). In the TEP, the two sides identified a number of broad areas in which they committed to work together in order to increase trade, avoid disputes, address disagreements, remove barriers and achieve mutual interests. These areas include: technical standards, agriculture, intellectual property, government procurement, services, electronic commerce, environment and labor. In addition, the U.S. and EU agreed to put an emphasis throughout the initiative on shared values, i.e. they agreed to more fully involve citizens and civil society on both sides of the Atlantic in trade policy so as to strengthen the consensus for open trade. Cooperation under the TEP will occur on a strictly bilateral basis, as well as in the context of multilateral activities such as in the WTO. The TEP Action Plan, endorsed by Leaders at the December U.S.-EU Summit in Washington, envisions achieving much of the bilateral activities identified under the initiative by the end of 1999.

New Transatlantic Agenda: President Clinton and European Union leaders at the U.S.-EU Summit held in Madrid in December 1995 sought to reaffirm the strong historic relationship between the United States and Europe, and to promote their vision of a post-Cold War Europe united around the principles of democracy and free markets. They embodied their commitment in an initiative called the New Transatlantic Agenda (NTA). This initiative seeks to deepen transatlantic relations by initiating specific joint U.S.-EU actions to address global economic, political, humanitarian, and environmental challenges more effectively. The 1995 NTA Action Plan included a commitment on the part of the United States and the EU to expand bilateral trade through an initiative called the New Transatlantic Marketplace (which later evolved into the Transatlantic Economic Partnership).

By the end of 1997, many of the economic steps envisioned in the New Transatlantic Agenda were accomplished, including the multilateral Information Technology Agreement, the WTO basic telecommunications and financial services agreements, and the bilateral U.S.-EU Mutual Recognition Agreement.

Public Dialogues: Important companions to both the Transatlantic Economic Partnership and New Transatlantic Agenda initiatives are the various private dialogues among European and American businesses, labor organizations and environmental and consumer groups. The first of these to be established, the Transatlantic Business Dialogue (TABD), is a forum in which top American and European business leaders can meet to discuss ways to reduce barriers to U.S.-European trade and investment. Other dialogues – the Transatlantic Labor Dialogue (TALD) and the Transatlantic Consumer Dialogue (TACD), along with a possible dialogue among U.S. and European environmental groups – start from a similar premise, i.e., that corresponding organizations on both sides of the Atlantic should share views and, where possible, present joint recommendations to governments in both the U.S. and the EU on how to improve transatlantic relations and to elevate the debate among countries in multilateral fora. The United States is committed to the full participation of civil society in the trade policy process and intends to cooperate closely with all the dialogues as it works to implement the TEP initiative.

Standards, Testing, Labeling, and Certification

A process of harmonization of standards is underway within the EU. The U.S. Department of Commerce anticipates that EU legislation covering regulated products will eventually affect 50 percent of U.S. exports to Europe. Given the enormity of this trade, EU legislation and standardization work in the regulated areas is of considerable importance. Although there have been improvements in some respects, a number of problems related to this evolving EU-wide legislative environment have caused concerns to U.S. exporters. These include: lags in the development of EU standards; lags in the drafting of harmonized legislation for regulated areas; inconsistent application and interpretation by Member States of the legislation that is in place; overlap among directives dealing with specific product areas; grey areas among the scope of various directives; and unclear marking and labeling requirements for these regulated products before they can be placed on the market.

The United States and the EU have begun implementation of an Mutual Recognition Agreement (MRA), which is designed to reduce unnecessary conformity assessment procedures. Once fully implemented, the MRA will permit a U.S. exporter to conduct various conformity assessment procedures (such as testing and inspection) in the United States according to the requirements of the EU, and vice versa. The programs and sectors covered by the current MRA includes: network and electromagnetic compatibility (EMC) for telecommunications and information technology equipment and radio transmitters; EMC and electrical safety for electrical and electronic products; good manufacturing practices inspections for pharmaceutical products and certain medical devices; product assessment for medical devices; and safety of recreational craft. The sectors covered by the MRA represent nearly $50 billion of annual two-way trade between the United States and the EU.

Intellectual Property Rights

At least five EU IPR measures announced in 1988, which were deemed essential to implementation of the internal market, have been enacted. These include directives on software; data bases; rental and lending rights; harmonization of copyright laws in satellite broadcasting and cable retransmission; and harmonization of the duration of copyright and certain related rights. However, progress remains slow on other directives in the copyright area, including directives on home copying and reprography. Some of these directives establish rights based on reciprocity, rather than on national treatment. Developments in the copyright area are being monitored closely, and senior U.S. officials have intervened a number of times to discourage the EU from adopting directives establishing rights based on the principle of reciprocity.

Copyright protection and the enactment of WTO consistent legislation in a number of EU member states remains inadequate, with seven EU member states having been cited during the 1998 Special 301 process. On May 1, the U.S. initiated WTO dispute settlement proceedings against Greece and the European Union regarding the high rates of piracy in Greece. Greece was first placed on the Special 301 "priority watch list" in November 1994 and remains on the list. As a result of the 1998 review, Italy was elevated to the Special 301 "priority watch list" due to extensive copyright piracy and trademark counterfeiting. The Italian parliament is considering a new anti-piracy law that would significantly strengthen enforcement and raise penalties. The United States in 1997 initiated WTO dispute settlement procedures against Sweden and Denmark, for failing to provide provisional relief in civil enforcement proceedings, and against Ireland for failure to enact TRIPS-consistent copyright legislation. In December 1998, the U.S. and Sweden announced settlement of the dispute following Sweden's enactment of legislation which brought its laws into compliance with TRIPS. Ireland has committed to accelerate its work on a new copyright law and passed interim legislation in 1998 addressing pressing enforcement issues.

The European Union, as an entity, remained on the "priority watch list" due to several objectionable practices, including continued denial of national treatment to US intellectual property right holders with respect to the distribution of revenues collected in association with blank tape levies and public performances and domestic content restrictions in certain member states that deny market access opportunities for U.S. shareholders.

Telecommunications

Europe is in the process of implementing wide-ranging liberalization in its telecommunications services market. The European Community and Member States, with limited exceptions, committed to provide market access, national treatment and fair regulatory practices as part of the WTO Basic Telecommunications Agreement, which went into effect on February 5, 1998. Greece, Ireland, Portugal and Spain made subsector-specific reservations in the WTO agreement, mirroring derogations granted under EU law that permit from one to five years extra time before the introduction of competition. However, Ireland and Spain have abandoned these derogations and, as of December 1, 1998, have opened their markets to full competition.

The record of implementation under the agreement so far is mixed. Many Member States have begun licensing of new entrants, along with taking the steps necessary to compel former monopolies to meet pro-competitive obligations set forth in the WTO Agreement and, in more detailed EU directives. However, some governments have been slow to adopt or put in place the legislative and regulatory mechanisms necessary to implement EU directives. The European Commission's competition directorate, DG-IV, has taken an active stance in bringing actions for non-compliance with EU directives in order to compel implementation.

Since 1985, the United States has pressed European nations to open their markets to foreign telecommunications equipment. Important items of concern remain, such as the discriminatory procurement policies of some state-owned telecommunications firms. For example, telecommunications administrations in some EU countries still procure their network equipment from domestic national suppliers whenever possible.

The United States is concerned that the adoption in December 1998 of a Common Position on the Introduction of Universal Mobile Telecommunications Services (UMTS) does not adequately reflect the advent of competition under the World Trade Organization (WTO) Basic Telecommunications Agreement. While the stated intention may be to assure a minimum level of inter-operability in Europe, the fact remains that the Common Position confers regulatory certainty and therefore a market advantage upon the subset of third generation mobile telecommunications technologies eventually authorized by the European Telecommunications Standards Institute to provide UMTS. In accordance with the European Community and Member States' WTO commitments, EC Member States should instead license and assign radio spectrum to the maximum number of service providers without regard to technology, based on the third generation standards that emerge from industry-led negotiations in the International Telecommunication Union (ITU). The ITU process is expected to be completed within 1999.

EU Implementation of Uruguay Round Grain Tariff Commitments

During the Uruguay Round, the United States negotiated a concession providing a ceiling on the duty-paid import price of grains into the EU. Subsequently, the EU established a reference price system for grain imports. The reference price system deprived U.S. exporters of the significant duty reductions that they expected to receive on high-value grains, such as malting barley and packaged rice.

Following a request for a WTO dispute panel by the United States in late 1995, the United States and the EU reached an agreement on brown rice and malting barley. The EU originally committed to establish a cumulative recovery system (CRS) on brown rice, and a side commitment to establish a system that would permit imports of a limited amount of malting barley at 50 percent or less of the duty that would otherwise be charged. The CRS regime expired in December 1998 and has been replaced by a temporary system which provides for reduced duties. Discussions continue with EU officials on a permanent replacement for the CRS. Regulations for the malting barley TRQ were published in April 1997 and an agreement on import duties was reached in January 1998.

EU Banana Regime

On July 1, 1993, the EU, as part of its Single Market exercise, implemented a new banana regime to replace individual member state rules for banana imports. Elements of the new regime include a tariff-rate quota which limits imports of bananas from Latin America, and a licensing system that burdens Latin American banana imports and favors EU firms to the detriment of Latin American and U.S. interests. The EU blocked adoption of a 1994 GATT panel report against its regime. After efforts to resolve this issue through negotiations, the United States in 1996 joined Ecuador, Guatemala, Honduras, and Mexico in a WTO dispute settlement panel process. The WTO panel and subsequent Appellate Body found the EU regime violated many provisions of the GATT and GATS. The EU has failed to implement a WTO-consistent regime by the WTO-mandated deadline of by January 1, 1999. The United States has sought WTO authorization to suspend concessions immediately following the arbitration, which the EC requested, of the amount of the U.S. suspension of concessions.

Approval of Biotechnology Products in the EU

Existing legislation covering biotechnology in the EU has proven to be unpredictable, cumbersome, and non-transparent. In 1996, the EU ultimately approved market access for a variety of glyphosate-tolerant soybeans and a variety of Bt corn. In 1997, three varieties of genetically modified corn harvested in the United States experienced significant delays in approval from the EU. Approval applications for these three products had been first submitted as long as two years earlier. When the applications began to move in the fall of 1997, a new scientific review was inserted in the approval process thereby delaying final approval. A newly created scientific committee gave its approval to the three products in February 1998. Final EU approval was not obtained until August 1998. The United States lost $200 million in corn sales in 1998 because of the delay, and additional losses are possible in 1999 because of continued approval delays for other genetically engineered corn varieties.

The United States continued to express concerns about aspects of the EU's regulatory processes for bioengineered food products and is continuing a dialogue with the EU on these issues. Both sides agreed in late 1998 to use the Transatlantic Economic Partnership to set up a Biotechnology Working Group to identify and address differences in regulatory processes that delay the approval process in the EU. The first meeting of the working group took place in February 1999.

Ban on Growth Promoting Hormones in Meat Production

The EU has banned the use of certain growth promoting hormones in livestock production. This ban, with limited exceptions, has been applied to meat and meat products imported into the EU since January 1, 1989. The ban has effectively limited most U.S. red meat and meat product exports to the EU. Because the EU has insisted on maintaining the hormone ban, in 1996 the United States initiated formal WTO dispute settlement proceedings with the EU.

The panel in the hormones dispute issued its final report to the Parties on June 30, 1997. The panel found in favor of the United States, finding that the EU's ban on imported meat from animals treated with certain growth-promoting hormones is inconsistent with the EU's obligations under the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement). In particular, the panel's report affirmed that the EU's ban is not based on science. It is not based on a risk assessment.

The EU appealed the Panel's findings, but the Appellate Body in its final report on January 16, 1998, while not sustaining some elements of the Panel's findings, upheld the finding that the EU's ban on imported meat from animals treated with certain growth-promoting hormones is inconsistent with its obligations under the WTO SPS Agreement. In particular, the Appellate Body affirmed that the EU's ban is not based on a risk assessment. The EU has until the WTO-mandated deadline of May 13, 1999, to comply with the WTO rulings.

Monitoring of the Large Civil Aircraft Agreement

The United States held formal consultations with the European Commission in January and July 1998 under the terms of the 1992 U.S.-EU Agreement Concerning the Application of the GATT Agreement on Trade in Civil Aircraft on Trade in Large Civil Aircraft. This Agreement established special limits over government support to large civil aircraft of 100 seats or more. At those meetings, the parties exchanged information under the terms of the Agreement's transparency provisions on direct and indirect government support and discussed current developments with respect to government involvement in large civil aircraft manufacture and marketing, such as government launch aid for new Airbus aircraft. Ideas for improving the operation of the agreement were also examined.

Voluntary Eco-Labeling Scheme

The European Council in 1992 approved a voluntary program that permits a manufacturer to obtain an eco-label for a product when its production and life-cycle meet general and specific criteria established for that particular purpose. U.S. producers have expressed concerns that the eco-labeling program, although voluntary, could create barriers to U.S. exports. U.S. and EU technical and policy officials consulted in 1995 and 1996 to discuss the EU process for developing criteria and to address specific U.S. industry concerns. EU eco-label criteria have been published for twelve consumer product categories: washing machines, dishwashers, soil improvers, toilet paper, paper towels, laundry detergents, light bulbs, paints and varnishes, bed linens and T-shirts, photocopy paper, and refrigerators. In 1997, the Commission planned to develop criteria for converted paper products, woolen and synthetic textiles, personal computers, and footwear. The converted paper criteria were never published because of opposition from some member states. The United States had seen some responsiveness to U.S. industry concerns with respect to the criteria and the U.S. and EU again discussed ecolabeling in October 1998 as part of the U.S.-EU High Level Consultations on Environmental Issues. However, problems remain. The U.S. intends to continue to monitor closely the development of the EU eco-labeling criteria and the proposed revisions to the program's regulatory basis to ensure that this program does not place U.S. producers at an unfair disadvantage.

Canned Fruit

The U.S. cling peach industry alleges that the displacement of U.S. canned peaches in the United States and in third country markets is due to EC programs that give a competitive advantage to their canned fruit industry, primarily to the Greek canned peach industry. Damage to the interests of the U.S. canned peach industry caused by EC programs is a long-standing issue. In order to better understand the extent and nature of the program affecting peach processing in the EU, the United States organized a coalition with five other canned peach producing countries (Argentina, Australia, Brazil, Chile and South Africa) and held informal consultations with the EC Commission in February 1997. As a result of these consultations, the EC subsequently provided the United States with additional data concerning their support programs for peach growers and processors. The United States joined with 13 other countries in challenging the EC on its canned peach regime at the March 1998 meeting of the WTO Committee on Agriculture (COA). Informal consultations were held in June 1998, at which the EC was pressed for information about its subsidy regime and its displacement of other exporters. The EC has expressed a willingness to meet with the canned peach producing countries in early March 1999. In February 1999, USDA's Economic Research Service is expected to release a report analyzing the factors underlying competitive positions of the U.S. and EC canned peach industries. The United States and interested exporting countries are scheduled to meet in February to discuss the situation.

Veterinary Equivalence

As a part of the Single Market initiative, the EU harmonized its animal and public health standards among Member States. In harmonizing these standards, the EU introduced new import controls for animal and animal products, which threatened to disrupt U.S. exports to the EU. On April 30, 1997, USDA Secretary Glickman announced that the United States and the European Union had reached an agreement on an overall framework for recognizing each other's veterinary inspection systems as equivalent. The agreement is expected to open new opportunities for red meat exports and preserve most pre-existing trade in products such as pet food, dairy and egg products. Without this agreement, U.S. exports of some products, including egg products and dairy products, would have been blocked from the EU market unless U.S. industries invested in costly adjustments to their facilities to comply with each EU internal market requirement. The agreement is expected to be finalized in July 1999, when the EU is expected to complete its internal approval process and the U.S. proposes regulations to permit imports of live animals and animal products from disease free areas within the EU.

While conditions for trading poultry and poultry products will be less restrictive under the agreement, U.S. poultry plants using anti-microbial treatment are not able to ship to the EU. The EU will not accept our use of anti-microbial treatments such as chlorine despite the fact that such treatments are an important element in modern poultry and red meat processing.

SRM Ban

On July 30, 1997, the European Commission adopted Commission Decision 97/534/EU, commonly known as the SRM ban. The goal of the ban is to avoid health risks related to Transmissible Spongiform Encephalopathies (TSEs), such as, Bovine Spongiform Encephalopathy (BSE or "mad cow disease") or new variant Cruetzfeld-Jakob Disease (nvCJD). The ban prohibits the use of specified risk materials (defined as the skull, including the brain and eyes, tonsils, and spinal cord of cattle, sheep and goats aged over one year and the spleens of sheep and goats) in any products sold in the European market.

If implemented as currently written, the Decision could unnecessarily result in shortages of critical medications in Europe and cause significant disruption of international trade. The Decision threatens U.S. exports to the EU of pharmaceuticals, cosmetics, gelatin, tallow and its derivatives, pet food and many other food and consumer products. The estimated trade impact for the United States exceeds $4 billion in exports; sales of products manufactured in Europe by U.S. companies may also be affected. In addition to the trade impact, U.S. public health agencies are concerned that the measure would cause international shortages of needed pharmaceutical products containing gelatin and tallow, adversely affecting public health.

The United States continues to press the EU for an exemption from the SRM ban based on the fact that BSE does not exist in the United States, and that U.S.-sourced products are therefore safe. The EU delayed implementation of its SRM ban several times with the most recent being to January 1, 2000. During these delays, the EU was working to amend the ban to avoid a public health crisis and unnecessary trade disruption.

U.S.-EC Wine

The United States and the EC Commission continued a series of talks in 1998 to determine whether negotiations on wine issues could be launched with a reasonable chance of succeeding. A major U.S. concern has been the failure of the EC to fulfill all its obligations under the 1983 Wine Accord, especially the commitment to review and approve a number of wine making practices approved for use in the U.S. The EU's requirement for annual derogations for some of these practices has been disruptive to U.S. exports. The U.S. has been unwilling to negotiate under conditions in which it would likely confront expiration of the derogations during the negotiations, and also has been unwilling to agree to concessions on semi-generic wine names when it has no assurance on long-term EC approval of U.S. wine making practices. A major EC concern is the use of semi-generic names on some U.S. wines. Other issues include tariffs, approval procedures for labels, the use of certain terms on labels, and import certification.

On December 17, 1998 the EC Council approved an extension of the existing derogations for U.S. wine making practices for 5 years or until an agreement is reached, whichever comes first. This opens the way for talks toward an agreement that will greatly benefit U.S. and EU wine industries.

Central Europe and the Newly Independent States

During 1998, most Central European countries continued to make progress in their efforts to transform formally centrally planned economies into market-oriented systems. Since the formal dissolution of the Soviet Union at the end of 1991, each of the new independent republics has also been working towards this goal; however, progress in some of these countries is limited. The nature of the reforms adopted and the speed with which they are being implemented varies considerably from country to country.

The United States has actively supported political and economic reforms in Central Europe and the New Independent States (NIS) of the former Soviet Union. The United States continues to provide financial, technical, and administrative assistance designed to support movement toward democracy and market economies.

A primary focus of U.S. efforts has been to construct a framework for the rapid expansion of trade and investment between the United States and Central Europe and the NIS. This framework includes negotiating trade agreements to extend Normal Trade Relations (formerly referred to as "most-favored nation" or "MFN") tariff treatment and intellectual property rights (IPR) protection, extending Generalized System of Preferences (GSP) benefits to eligible countries, encouraging adoption of WTO provisions in these countries' trade regimes, and negotiating Bilateral Investment Treaties which guarantee compensation for expropriation, transfers in convertible currency, and the use of appropriate dispute settlement procedures.

Normal Trade Relations (NTR) Status

All Central European countries and NIS republics, except Serbia and Montenegro, receive NTR tariff treatment. Under Title IV of the Trade Act of 1974 (the Jackson-Vanik provisions), the President is required to deny NTR tariff treatment to any non-market economy which was not eligible for such treatment and which the President determines denies or seriously restricts or burdens its citizens' right to emigrate, unless the President determines that a waiver of the requirement will substantially promote the legislation's objectives, or has reported to Congress that an affected country complies fully with the legislation's emigration requirements. In addition, the Jackson-Vanik provisions require affected countries to have a trade agreement with the United States, including certain specified elements. Title IV applies to Russia and the eleven other NIS republics, Albania, Cuba, Mongolia, the People's Republic of China, Vietnam, and North Korea. The President has determined that Albania, Mongolia, Russia and all of the other NIS except Belarus are in full compliance. Belarus and China continue to receive NTR tariff treatment under annual waivers. Cuba and North Korea do not have NTR status. Vietnam received its initial waiver in 1998, but a trade agreement has not yet been concluded. Congress must enact a law to terminate application of Title IV to a country.

The United States has trade agreements with all NIS republics and all Central European countries. The trade agreement between the United States and the Former Socialist Federal Republic of Yugoslavia continues to apply to the five successor states: Bosnia and Herzegovina, Croatia, the Former Yugoslav Republic of Macedonia, Slovenia and Serbia-Montenegro (FRY).

In December 1991, Congress terminated application of Title IV to Estonia, Latvia, and Lithuania. Pursuant to specific legislation, the President also terminated application of Title IV to the following countries and accorded them unconditional NTR status: the Czech and Slovak Federal Republic (now the Czech Republic and Slovakia -- April 1992), Hungary (April 1992), Bulgaria (September 1996), and Romania (November 1996). Title IV never applied to Poland or the former Yugoslavia. As part of U.S. sanctions policy, the President revoked NTR from Serbia and Montenegro; in 1996, certain sanctions were lifted pursuant to the peace accords negotiated in Dayton, Ohio, although NTR tariff treatment was not restored.

Protection for Intellectual Property Rights

The trade agreements with Central Europe and NIS republics include provisions on IPR protection. Many of the NIS countries still have not fully implemented the IPR provisions of the trade agreement; the U.S. continues to work with them to bring them into compliance. IPR issues in three countries merit special mention.

Bulgaria

Bulgaria was elevated to the "Priority Watch List" during an out of cycle Special 301 review in January 1998. At that time the Government was informed that should it fail to make substantial progress toward combating piracy of optical media (CDs and CD-ROM) it would be identified as a "Priority Foreign Country." During 1998, Bulgarian authorities undertook a series of strong enforcement measures to reduce significantly the production and export of pirated optical media. Because of these efforts on the part of Bulgarian authorities, Bulgaria was moved to the Special 301 Watch List in November 1998. There are still reports that pirate production and export has continued, albeit at substantially reduced levels. In addition, there is evidence that some of Bulgaria's pirate producers have relocated their operations to other countries, such as Moldova, Montenegro, Serbia, and Ukraine, and are exporting their illegal product to Bulgaria.

The Russian Federation

Russia has enacted comprehensive laws to protect IPR, but a few major deficiencies remain. Most notably, enforcement of IPR remains a pervasive problem. The prosecution and adjudication of intellectual property cases remain weak and sporadic, there is a lack of transparency, and a failure to impose deterrent penalties. Customs administration also needs significant strengthening. Piracy of U.S. films, videos, sound recordings, and computer software is rampant. Russia has yet to provide protection, as required by our bilateral trade agreement, to pre-existing U.S. copyrighted works and sound recordings still under protection in the United States. Some U.S. companies have had difficulty registering well-known marks, and trademark infringement is reportedly on the rise. In April 1998, Russia was placed on the Special 301 "Priority Watch List" because of these and other problems.

In 1998, the U.S. Government began a USG-wide IP law enforcement technical cooperation program with Russia which was proposed as part of the U.S.-Russia Joint Commission chaired by Vice President Gore and the Russian Prime Minister. In September and October of 1998, Russian judges, law enforcement personnel, prosecutors and representatives from business and the media attended three weeks of IP law enforcement seminars in both Washington and Moscow.

Ukraine

Ukraine has made significant progress in enacting IPR legislation, although a few major deficiencies remain. Enforcement of IPR protection remains weak and sporadic, and piracy of U.S. films, videos, sound recordings, and computer software is widespread. Registration and protection of trademarks has also been a problem. Ukraine has yet to provide protection, as required by our bilateral trade agreement, to pre-existing U.S. copyrighted works and sound recordings still under protection in the United States. Another major deficiency is the lack of authority on the part of Ukrainian Customs for border enforcement. In July 1998, the United States-Ukrainian working group on IPR convened to discuss these and other issues.

The Generalized System of Preferences

Under the GSP program, developing countries are eligible to receive duty-free access to the U.S. market for many items, if they meet certain statutory criteria. In addition, a country must first have NTR status to apply for GSP treatment. Most Eastern European countries have been beneficiaries of this program since the early 1990s. Until 1993, however, most of the New Independent States were not eligible for GSP benefits because they were considered successor states of the former USSR, and therefore prohibited by statute from receiving GSP program benefits. The prohibition against granting GSP to the successor states was removed as part of the 1993 Budget Act. By the beginning of 1996, all of the former Soviet republics that requested beneficiary status received GSP, although Azerbaijan, Georgia, Tajikistan, and Turkmenistan have never requested GSP and therefore do not benefit from the program. In late 1997, Georgia petitioned for eligibility as a GSP beneficiary country, and that petition is currently being reviewed. Estonia, Latvia, and Lithuania are not considered successor states of the USSR, and therefore became beneficiaries of the GSP program in February 1992. I n 1997 the AFL/CIO petitioned USTR to remove Belarus eligibility for GSP because of violation of worker rights. A public hearing was held in November 1997 as part of USTR's ongoing review.

WTO Accession

Most Central European and NIS countries are members or are in the process of acceding to the WTO. Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia, and Slovenia are already members of the WTO. Following successful negotiations, the WTO General Council on October 14 ,1998 approved accession packages for the entry of the Kyrgyz Republic and Latvia. These countries will become WTO members following ratification by their national parliaments on January 20, 1999 and February 11, 1999, respectively. WTO accession working parties have been established for Albania, Armenia, Azerbaijan, Belarus, Croatia, Estonia, the former Yugoslav Republic of Macedonia, Kazakhstan, Lithuania, Moldova, the Russian Federation, Ukraine and Uzbekistan. The United States supports the accession of these countries into the WTO on commercial terms and on the basis of implementation of WTO provisions. WTO accession and the adoption of WTO provisions can be an important method of supporting economic reform. The United States has provided technical assistance, in the form of short- and long-term advisors, to many of the countries in support of the WTO accession process.

Bilateral Investment Treaties

Bilateral Investment Treaties (BITs) protect U.S. investment abroad in countries where US investors' rights are not protected through existing agreements such as our treaties of Friendship, Commerce and Navigation. The United States has placed a priority on negotiating BITs with countries undergoing economic reform and where we believe we can have a significant impact on the adoption of liberal policies on the treatment of foreign direct investment. They also lay the policy groundwork for broader multilateral initiatives in the OECD and, eventually, the WTO.

BITs provide that US companies will be treated as favorably as their competitors (by providing the better of national or NTR treatment). In addition they: (1) establish clear limits on the expropriation of investments and ensure prompt, adequate, and effective compensation when expropriation occurs; (2) guarantee US investors the freedom to transfer funds in and out of a country without delay, using a market rate of exchange, (3) restrict the ability of local governments to require inefficient and trade distorting practices by prohibiting performance requirements such as local content or export quotas, (4) give US investors the right to submit an investment dispute with the Treaty partner's government to international arbitration, and (5) give US investors the right to engage the top managerial personnel of their choice, regardless of nationality.

The United States has BITs in force with six NIS countries -- Armenia, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, and Ukraine. Azerbaijan, Belarus, Russia, and Uzbekistan have also signed BITs with the United States, but the formal process of ratification has not been completed. Discussions for BITs are also underway with most of the other NIS republics.

In Central Europe, the United States has BITs in force with Albania, Bulgaria, the Czech Republic, Estonia, Latvia, Poland, Romania, and Slovakia. The BITs with Croatia and Lithuania have been signed but await ratification by both sides. The United States recently has entered into discussions aimed at negotiation of a BIT with Slovenia.

Commercial Space Launch

Russia

On September 2, 1993, Vice President Gore and Russian Prime Minister Chernomyrdin signed an agreement on Russia's participation in the commercial space launch market. The agreement gives Russia an opportunity for its space launch industry to participate in the international launch services market and offers Western satellite companies an additional source of competitive launch capacity. It also provides general rules of the road for fair competition in commercial space launches and requires Russia to charge prices comparable to those of Western launch providers for similar services during the period of its space launch industries' transition to market-based operations. As originally concluded, the agreement afforded Russia the opportunity to compete for contracts to launch up to eight commercial payloads to geosynchronous earth orbit (GEO) for international customers (in addition to the INMARSAT 3 satellite and three launches to low-earth-orbit for the Iridium system) between signature and December 31, 2000. On January 30, 1996, Vice President Gore and Prime Minister Chernomyrdin signed an agreement that amended the September 2, 1993, text to allow Russia the opportunity to launch up to 15 commercial payloads (in addition to INMARSAT 3) to GEO, with four more launches possible if future market demand proves more robust than anticipated. The amendments also give Russia additional flexibility on pricing in exchange for greater transparency in price setting, and liberalize rules governing the launch of satellites to low-earth orbit. The amendments brought the Russian space launch agreement roughly into conformity with the space launch agreements the United States has negotiated with Ukraine and China since September 1993.

In late 1998, the Administration informed the Russian Government that it could not foresee increasing the quantitative restriction on GEO launches until Russia showed greater cooperation in preventing the transfer of missile technology to nations such as Iran.

Ukraine

On February 21, 1996, Vice President Gore and Ukrainian President Kuchma signed an agreement on Ukraine’s entry into the commercial space launch market. The agreement with Ukraine is meant to serve the same basic function as the pre-existing agreements with China and Russia. The agreement affords Ukraine the opportunity, between signature and December 31, 2001, to launch up to 16 commercial payloads to GEO for international customers (11 of which must be reserved for a joint venture involving a U.S. company). In addition, Ukraine will have the opportunity to launch up to four more commercial payloads (three of which must be reserved for a joint venture with a U.S. firm) to GEO if future market demand proves more robust than anticipated. The liberalized rules governing pricing and launches to low-earth-orbit contained in the China and amended Russia agreements are mirrored in the agreement with Ukraine.

EU Association Agreements

The United States strongly supports the integration of the Central European countries (CEC) into Western Europe. Most of the CECs have concluded Association Agreements (now called Europe Agreements) with the EU. The agreements are meant to lead eventually to full EU membership for the CECs concerned. They include tariff preferences both for EU imports from the CECs, as well as for CEC countries' imports from the EU, with the latter to be phased in over a period of years. During the interim period prior to accession, the United States wants to ensure that these preferences do not unreasonably discriminate against U.S. exports to the region.

The United States has been participating in a review, conducted by the WTO Committee on Regional Trade Agreements, of the Association Agreements to examine whether they are consistent with WTO provisions, including services obligations under the GATS. To better understand the effects of these agreements, USTR has also asked the International Trade Commission to conduct a comprehensive study of the trade effects of the association agreements, pursuant to section 332(g) of the Tariff Act of 1932. The ITC study is due to be completed in mid-April, 1999. In close consultation with industry, we will continue to raise specific issues as they arise with the CEC governments. For example, the U.S. and Polish Governments established in December 1997 an ongoing bilateral consultative mechanism on trade issues related to Poland's prospective EU membership, including the impact of its Association Agreement on U.S. commerce. We have also pursued consultations with other CEC governments. As a result of these efforts, Slovenia and, to a lesser extent, Poland lowered MFN tariffs on specific vehicle imports, providing more equitable access for non-EU exporters.

Aircraft Market Access in Russia

In 1996, the United States and Russia concluded a joint MOU that addresses U.S. concerns about access to the Russian civil aircraft market and the application of international trade rules to the Russian aircraft sector. Under the MOU, the Russian Federation confirmed that it will become a signatory to the Agreement on Trade in Civil Aircraft. In the interim, the MOU commits the Russian Federation to provide fair and reasonable access for foreign aircraft to its market. The Russian Government agreed to take steps, such as the granting of tariff waivers and the reduction of tariffs, to enable their airlines to meet their needs for U.S. and other non-Russian aircraft on a non-discriminatory basis. To date, Russian airlines have been able to import approximately 20 non-Russian aircraft under the MOU. In consultations in early 1997, the United States raised concerns about the complete implementation of the MOU. Senior Russian officials reaffirmed their commitment to it. In 1997, U.S.-produced large civil aircraft were sold and leased to airlines in the Russian Federation under the terms for fair access provided by the MOU.

During consultations in mid-1998, U.S. officials raised objections to the Russian Government's recently enacted resolution #716 which sets conditions for the reductions and exemptions of customs duties on imports of aircraft, engines and flight simulators. The principal measures require Russian airlines to commit to purchasing/leasing Russian-made aircraft equivalent to three times the amount of the customs duties to be waived in order to receive duty reductions and exemptions for the purchase/lease of foreign-manufactured aircraft and to conclude an investment agreement with the Ministry of Economics. During the course of 1998, tariff waivers were granted to Aeroflot for purchases of foreign aircraft under these conditions. This resolution conflicts with the 1996 U.S. - Russia Joint MOU which provides for unconditional tariff waivers on imports of aircraft. The United States opposes the resolution and continues to urge the Russian Government to implement the MOU.

Russian Restrictions on Vodka and Ethyl Alcohol Imports

Russia maintains high tariffs and excise taxes on imported spirits, and in 1997 imposed an extensive regulatory scheme for the import and sale of alcoholic products on the Russian market. This resulted in a dramatic contraction of U.S. vodka exports to Russia, which fell from $4.4 million in 1996 to $110,000 in 1997. In December 1997, the Russian Government imposed new licensing fees for distribution of alcohol products which discriminate severely against imported products. We also have concerns about application of excise duties, which U.S. exporters believe have not been equitably applied. In late 1998, the Russian Government further tightened restrictions on marketing of alcohol, under a new resolution, which envisages creating a state monopoly on the manufacture and state control over the distribution of alcohol of 28 proof and above.

In January 1999, a new law on state regulation of alcohol and alcoholic production was signed by the President, which establishes further barriers to trade in this sector. The new law establishes quotas, limiting imports of alcoholic products (other than wine, cognac and brandy, and beer) to 10 percent of Russian annual consumption. The new law also establishes extremely onerous conditions for receipt of export licenses. In addition, the Russian Government has submitted to the Duma (lower house of parliament) a new draft law that would ban the import of ethyl (pure) alcohol for three years. The United States opposes this restrictive regime and continues to urge the Russian authorities to adopt nondiscriminatory treatment in this sector.

Potential Restrictions on Tourism and Insurance Sectors

The United States was active in advocating against proposed Russian legislation in these two sectors which could potentially have deprived U.S. investors and services providers of meaningful market access. Following timely U.S. intervention, market-access restricting draft Amendments to Russia's Tourism Law, which passed by the Russian Parliament in late 1998, were subsequently vetoed by President Yeltsin. In addition, we expressed concern that draft amendments to the "Law on Foreign Investment in the Russian Federation," which passed the Duma and Federation Council in July 1998, would have restricted or prohibited foreign investment in a wide range of sectors, including tourism and insurance. These also were vetoed. While we have registered our concerns with positive effect, forces in the Russian Parliament may still pursue similarly restrictive legislation. We will continue to monitor carefully legislative developments in these areas.

Russian Product Standards, Testing, Labeling and Certification

U.S. companies still cite product certification requirements as a principal obstacle to U.S. trade and investment in Russia. In the context of Russia's WTO accession negotiations, we continue to urge Russia to bring its standards and certification regime into compliance with international practice. The Russian Government is now attempting to put in place the necessary legal and administrative framework to establish standards procedures and processes for certification and licensing of products in Russia.

There has been some movement to eliminate duplication among regulatory agencies and to clarify categories of products subject to certification. However, businesses are still experiencing difficulties in getting product approvals in key sectors. Manufacturer declaration of conformity is now feasible under Russian law, but is not applied in practice. In 1998, the Russian State Committee on Standards adopted a new nomenclature of goods subject to mandatory certification, effective Jan 1, 1999, and the Russian Government has been moving to revise problematic legislation, as provided under its TBT action plan.

Certification is a particularly costly and prolonged procedure in the case of telecommunications equipment. In many sectors, type certification or self-certification by manufacturers is currently not possible. Veterinary certification is often arbitrary and needs to be more transparent and based on science. Russian phytosanitary import requirements for certain planting seeds (notably corn, soybeans and sunflowers) appear to lack scientific basis and have blocked imports from the United States. Discussions to ease or eliminate burdensome Russian requirements are ongoing.

Ukrainian Product Standards, Testing and Certification

Ukraine's product, certification, and licensing requirements continue to constitute a nontariff barrier to trade. The situation is increasingly acute. Although the Government of Ukraine agreed to a work plan drafted by the CTI, no progress has been made on implementation.

The current Ukrainian system represents a considerable deterrent to Ukraine's accession to the WTO.

Polish Product Standards and Safety Certification

On many occasions in the past several years, most recently in October 1998, the United States raised with the Polish Government a concern that Polish product standards and safety certification were technical barriers to trade. Poland's product standards and safety requirements are not based on international norms. U.S. companies have found that the process for obtaining the safety certificates is time-consuming, expensive and non-transparent. As a result of U.S. intervention, the Polish Government has again postponed the full implementation of new safety certification procedures until December 31, 1999.

Poland's zero tolerance for weed seeds in imports of grain and oilseeds significantly restricts U.S. exports to Poland. Several of the weeds included on Poland's quarantine list do not meet the international definition of a quarantine pest, and the United States has argued that these weeds should be removed from the list. In November 1998, U.S. and Polish officials discussed this issue in Geneva under the auspices of the WTO Secretariat. The United States again requested that Poland remove these weeds from its quarantine list or agree to a review of Poland's risk assessment by an independent panel of international experts. At this time, the United States is awaiting Poland's formal response.

Western Hemisphere

The Western Hemisphere is the largest regional destination for U.S. merchandise exports, accounting for nearly 44 percent of total U.S. goods exports in 1998, up from 42 percent in 1997. U.S. exports to Latin America increased approximately 6.3 percent in 1998. The region continues to be an attractive market for U.S. exports and investments, given that its governments on the whole have responded effectively to the challenges produced by the Asian economic crisis. Not surprisingly, hemispheric growth rates are expected to suffer a decline in 1999 due to global market turbulence. However, the Americas will continue to offer U.S. exporters and investors valuable opportunities. Given that many Latin American countries already have restructured key sectors, enacted reforms, and increased transparency through economic liberalization following the 1980's Latin American debt crisis and the 1995 Mexican peso crisis, the region should continue to offer a promising, market-oriented environment in which to do business. The United States will continue to encourage such reforms.

This economic restructuring, which characterized the region over the past decade, has enabled the U.S. to pursue the opportunities presented by dynamic hemispheric growth. At the 1994 Summit of the Americas in Miami, the 34 democratically-elected leaders of the region agreed to create a comprehensive Free Trade Area of the Americas

(FTAA) by 2005. At the April 1998 Santiago Summit the hemispheric leaders formally initiated the FTAA negotiations, based on the March 1998 San Jose Declaration of the hemisphere's trade ministers . The United States has played a key role in the FTAA process, moving it toward the Miami Summit's objective of concrete progress in constructing the FTAA by the end of the century. We are pressing for agreement on and implementation of a set of important business facilitation measures by FTAA countries by the end of 1999.

Concurrent with the FTAA process, many countries have sought to deepen and expand their trading arrangements. To give just a few examples, in 1998 Mercosur continued to pursue a free trade area (FTA) with the Andean Community (AC). Mercosur is also engaged in on-going preliminary technical FTA discussions with the European Union (EU) and has negotiated a Trade and Investment Cooperation Arrangement with Canada. Mexico is also pursuing an FTA with the EU, while Canada has concluded an FTA with Chile. Chile now has FTAs with every major economy in the hemisphere with the exception of the United States.

Meanwhile, the U.S. continues to work toward building the FTAA in a manner consistent with U.S. interests and with the objective of encouraging hemispheric growth. President Clinton demonstrated his commitment to the Americas through again traveling to the region, this time to Chile in April 1998. By pursuing the FTAA, and by vigorously enforcing the bilateral and multilateral agreements that the U.S. maintains in the region, in particular the North American Free Trade Agreement (NAFTA), the Administration seeks to expand economic opportunities for the United States in the Americas.

Canada

Canada is the United States' largest trading partner with more than $1 billion worth of goods and services trade crossing the border daily. The U.S. - Canada Free Trade Agreement and the subsequent NAFTA established a broad and extensive set of rules and obligations, creating more open commerce for most products and services. Bilateral problems, however, remain.

Discriminatory Magazine Practices: In 1997, the United States successfully challenged Canada's protectionist magazine regime in the World Trade Organization. A WTO panel found three components of Canada's magazine polices to be illegal under the *General Agreement on Tariffs and Trade* (GATT). The panel condemned (1) a ban, in place since 1965, on imports of magazines with advertising directed at Canadians; (2) a 1995 special excise tax on so-called Asplit-run@ magazines; and (3) discriminatory postal rates for imported magazines. After Canada appealed the panel's report, the WTO's Appellate Body found a fourth violation -- Canada's discriminatory postal subsidy program for Canadian-produced magazines. Canada had until October 30, 1998, to bring its measures into conformity with the WTO.

In time to meet its WTO-imposed deadline, Canada repealed its longstanding ban on split-run imports, discontinued the 1995 special excise tax on split-runs, eliminated the discrimination in its postal rates, and modified its postal subsidy program for magazines. At the same time, however, Canada introduced Bill C-55, which is designed to accomplish the same result as the import ban and excise tax -- keeping U.S.- and other foreign-produced split run magazines from competing fairly in the Canadian market.

Bill C-55 would prohibit U.S. and other non-Canadian publishing companies, on pain of criminal fines, from using the magazines they produce to advertise directly to Canadian readers.

Among the four measures the WTO condemned was a confiscatory 80% tax imposed by the Canadian Government on imported magazines carrying this type of advertising. The tax put U.S. and other imported magazines at a significant commercial disadvantage in comparison to Canadian-produced magazines. Having finally agreed to eliminate the tax on these advertisements, the Canadian Government is now proposing to ban these advertisements altogether. Canada also proposes to continue, in a slightly modified form, its postal subsidy for Canadian-produced magazines.

Substituting one form of protectionism for another ignores both the letter and the spirit of WTO rules. The Administration has called on the Canadian Government to refrain from enacting C-55 and is prepared to negotiate a solution that creates an open and fair market for U.S. magazines in Canada. If Bill C-55 is enacted, however, the Administration has indicated it will respond by denying U.S. trade benefits of an equivalent commercial effect.

Agriculture Agreement: On December 4, 1998, the United States and Canada entered into a record of understanding regarding several areas of agricultural trade. The agreement provides for a number of market opening measures while establishing a framework for continued consultations to resolve disputes and make more progress. The Administration views it as a first step in a major effort to advance U.S. interests in agricultural trade with Canada. Highlights of the agreement include: establishing quarterly consultations at which time the Canadians will provide export projections of grain sales to the U.S.; providing U.S. grain farmers improved access to the Canadian rail system; allowing U.S. farmers to ship directly to Canadian storage elevators; elimination of burdensome testing requirements for karnal bunt disease in wheat; amending Canadian animal health requirements to facilitate movement of U.S. hogs and cattle into Canada; and improved cooperation on cattle trade data, harmonization of pesticide and animal drug restrictions and continued consultations on potato trade.

Wheat: The U.S. wheat industry continues to have concerns with the pricing and marketing practices of the Canadian Wheat Board. In response, the Administration announced plans in December 1998 to enhance the monitoring of wheat to develop greater insight into Canadian Wheat Board sales practices in the U.S. Specifically, the U.S. Department of Agriculture is amending the end use certificate to collect additional information on types of wheat and improve enforcement. Also, the U.S. International Trade Commission expanded the tariff codes - at the request of the Administration - to capture wheat type, grade and protein levels in the tariff nomenclature. The information that is developed from these new measures will be scrutinized closely by the Administration, along with export projections of annual wheat shipments to the U.S. provided by the Canadian Government. This enhanced monitoring is in addition to the continuing monitoring of Canadian wheat, particularly durum, imports begun in 1994.

Dairy: In response to concerns raised by the U.S. dairy industry, USTR and the U.S. Department of Agriculture investigated Canada's dairy price pooling mechanism and other aspects of the import regime which could be in violation of Canada's obligations under the WTO. The United States, following the filing of a section 301 petition by the U.S. dairy industry in September 1997 accepted the petition and is pursuing WTO dispute settlement. New Zealand is also pursuing WTO dispute settlement on this matter. The U.S. Administration expects a final panel ruling in March 1999.

Potatoes: The Administration continues to raise concerns with Canada about their restriction on bulk shipments of potatoes. The December 4, 1998, record of understanding also calls on both parties to pursue resolution of this matter.

Furthermore, the record of understanding calls on the respective industries to recommend solutions to how regulatory differences and restrictions could be changed to facilitate trade.

Copyright Legislation: The Government of Canada has adopted amendments to its copyright law that discriminate against the interests of some U.S. copyright holders. Canada has established a public performance right for record producers and performers. It also has established a levy on blank audio recording media, the revenues from which are intended to compensate performers and producers for the performance and unauthorized home-taping of their works in Canada. The United States remains extremely concerned that U.S. performers and producers are denied national treatment with respect to these provisions and will closely monitor any future reform of Canada's copyright laws.

Softwood Lumber Agreement: The five-year U.S.-Canada Agreement on Softwood Lumber, the largest bilateral sectoral accord into which the U.S. has entered, was in its third year of operation in 1998. The Agreement allows British Columbia, Alberta, Ontario and Quebec (the major lumber-producing provinces) to export 14.7 billion board feet of lumber fee-free to the United States; shipments above that quantity are subject to export fees. At no point does the Agreement prohibit Canadian lumber shipments outright. The Agreement's market-responsive mechanism ensures a stable and plentiful lumber supply for U.S. consumers by allowing additional shipments of fee-free lumber in periods of peak demand.

On June 1, 1998, the Government of British Columbia (B.C.) changed the formula by which it calculates the administratively set timber prices, or "stumpage rates", it charges B.C. lumber mills. British Columbia thereby reduced stumpage rates by 16%. This effectively reduces the price B.C. lumber mills have to pay for the lumber they export to the United States. By this action, the Administration believes, British Columbia violated the U.S. - Canada Softwood Lumber Agreement.

On June 22, 1998, we requested consultations with the Government of Canada under Article V(1) of the Agreement. Consultations were held on July 10, 1998, but a mutually satisfactory resolution was not achieved. Because the Parties have failed to resolve this matter, the Administration initiated arbitral proceedings pursuant to Article V(3) of the Agreement. The United States filed its first submission in the softwood lumber dispute with Canada on December 30, 1998. Canada's first submission was filed on January 26,1999. Additional legal briefs will take place in February and March, followed by a hearing. A panel ruling is likely in April or May 1999.

Minnesota/Ontario Fishing: Ontario has disadvantaged the Minnesota tourism industry by limiting the fish catch of tourists who stay on the Minnesota side of certain lakes that straddle the U.S.- Canadian border. In addition, U.S. fishing guides and U.S. tourists overnighting in the U.S. are subject to more documentation requirements and licensing fees than Canadians and U.S. tourists overnighting in Ontario. The restrictions now apply to within 150 miles of the border, but Ontario has announced it may extend the restriction an additional 150 miles in 1999, thereby increasing significantly the economic harm to U.S. resort owners and fishing guides. USTR is working with Canada to address these practices.

Mexico

The NAFTA provides an unprecedented set of comprehensive market opening rules that have steadily expanded opportunities for U.S. goods and services in Mexico. In 1997, Mexico surpassed Japan to become our second largest merchandise export market. The rapid growth in two-way trade has benefitted many firms and workers in both countries. At the same time, bilateral concerns exist:

Standards: U.S. exporters have encountered problems arising from implementation of Mexican mandatory labeling and certification requirements affecting a broad range of products. These issues have been the subject of ongoing bilateral consultations and in the NAFTA Committee on Standards-Related Measures. The United States has repeatedly called on the Government of Mexico to recognize its obligation to publish changes in regulations with adequate time for public comment. Under Article 908.2 of the NAFTA, Mexico is obligated to recognize U.S. and Canadian certification bodies on a national treatment basis from January 1, 1998. Mexico announced it would honor that obligation, but did not recognize any U.S. certification bodies throughout 1998. Discussions with Mexico continue on this topic.

Intellectual Property Rights (IPR): Piracy and counterfeiting of U.S. intellectual property in Mexico continue to be serious concerns. In December 1997 Mexico passed a new law protecting semiconductor maskworks, meeting its NAFTA obligation to provide this protection by January 1, 1998. In May 1998, Mexico passed the implementing regulations for the new copyright law. The U.S.-Mexico bilateral IPR working group had been meeting regularly since January 1996 to promote IPR protection in a manner consistent with the NAFTA. In November 1998, Mexico announced a new anti-piracy campaign, providing greater penalties and greater resources for enforcement and training. The campaign in significant ways hinges upon Congressional action, which was not expected to occur prior to March 1999.

Agriculture: North American agricultural trade has grown significantly since the NAFTA.. Mexico is our third largest export market. For the last fiscal year, (October 1997-September 1998), total agricultural exports to Mexico increased by 17.3 percent, while exports to the rest of the world outside of NAFTA fell 6.3 percent. However, trade irritants exist. A major irritant has included Mexico's effort to limit the importation and domestic consumption of high fructose corn syrup. Among a number of efforts the Administration is pursuing to remedy this concern, USTR initiated a section 301 investigation (May 1998) into Mexico's efforts to limit domestic consumption of corn syrup. In addition, irritants include Mexico's *de facto* practice of allowing only 13 truckloads of swine to be imported each day through the port at Del Rio. New Mexican poultry regulations concerning avian influenza may become a serious impediment to trade. Technical experts are working to minimize the impact of these new regulations.

Telecommunications: Mexico's telecommunications market remains a source of concern in certain respects. For example, the Administration is urging Mexico to provide for international simple resale services. This practice denies competitive U.S. firms opportunities and impedes the development of cross border trade in this sector. The Administration has indicated it is preparing a potential WTO dispute settlement case in light of Mexico's failure to provide for this service.

Broom Corn Brooms: In November 1998, the President removed safeguard relief for the U.S. broomcorn industry that had been provided two years earlier. Mexico removed, effective January 1, 1999, the retaliatory tariffs it imposed on corn syrup, flat glass, wine, coolers, brandy, whisky, notebooks, flat glass and wooden furniture in response to the safeguard.

Antidumping: The United States is closely observing Mexico's use of anti-dumping procedures. In this regard, in addition to the WTO, the NAFTA Chapter 19 antidumping review process is a venue to encourage greater discipline in both original investigations and as a result of panel remand decisions. During the five years since the implementation of the NAFTA, nine panel reviews have been conducted concerning Mexican agencies' determinations. Five cases have been completed, three were terminated at the request of the participants, and only one is still active, involving high fructose corn syrup, which is also subject to WTO dispute settlement. Completed cases from the United States included polystyrene (1996), cut-length plate (1995), and flat coated steel (April 1998). The hydrogen peroxide and seamless steel tube cases were terminated.

Brazil and Southern Cone

Mercosur

The Common Market of the South, referred to as "Mercosur," from its Spanish abbreviation, is the largest preferential trade agreement in Latin America. It consists of Brazil, Argentina, Uruguay and Paraguay and represents over half of Latin America's GDP. Chile and Bolivia are Associate Members of the group. Mercosur was established in 1991, with the goal of creating a common market. Implementation of the Mercosur customs union commenced January 1, 1995, with the establishment of a common external tariff (CET), covering some 85 percent of intra-Mercosur trade. Convergence on excepted items is slated for completion by January 1, 2006.

Preliminary figures indicate that total U.S. exports to Mercosur were $27 billion in 1998, with a U.S. trade surplus of $12 billion. Over the past year, Mercosur faced challenges related to the world financial crisis, leading to a reduction in overall growth rates. GDP grew, on average, just under five percent in Mercosur in 1997, while early predictions for 1998 hover at less than two percent. Brazil, the largest economy in Mercosur and Latin America, was under the most pressure from the global economic situation. It received approval of an IMF loan package of over $41 billion in late 1998 to assist in responding to this financial pressure. In early 1999, the Brazilian Government devalued its currency by allowing the Real to float on the world currency market. Despite the difficulties brought by market turbulence, we continue to see this area as one filled with potential. The U.S. Government has strongly encouraged Mercosur not to respond to these financial pressures by backsliding on the trade liberalization that has led to increased prosperity in the hemisphere over the past decade.

The United States has continued to develop our trade relationship with this important trade group, both bilaterally and in multilateral fora. This effort has been most pronounced in the context of the Free Trade Area of the Americas (FTAA). The U.S. will continue to vigorously pursue its interests in Mercosur, particularly as Mercosur pursues trade negotiations with others, such as Canada, Mexico, the Andean Community (AC) and the European Union (EU), and as it deepens its institutional reach in areas such as services and government procurement.

Brazil

The United States enjoyed a trade surplus with Brazil in 1998 of $ 10 billion, even though exports fell $753 million between 1997 and 1998. Brazil's market accounts for approximately 24 percent of U.S. annual exports to Latin America and the Caribbean excluding Mexico, and over 56 percent of U.S. exports to Mercosur.

Wheat: In 1998, the United States and Brazil reached agreements on U.S. Hard Red Winter (HRW) wheat which reopened Brazil's market – a leading world importer of wheat. Imports from the United States were banned in 1996 due to certain plant diseases. A major achievement for the United States was Brazil's decision, based on strong scientific evidence presented in a pest risk assessment, to eliminate its phytosanitary restriction against the United States for TCK wheat fungus in April. In addition, in November, a bilateral Certification Protocol was signed allowing HRW wheat grown in the Great Plains, and exported through Mississippi and Gulf ports, to enter Brazil. Prior to the 1996, U.S. growers exported about 750,000 tons of wheat to Brazil. The 1998 agreement on TCK is viewed as the start of a closer working relationship on phytosanitary issues.

Autos: In March 1998, USTR signed an agreement with the Government of Brazil to terminate its TRIMS-inconsistent (Trade-Related Investment Measures) auto regime, enacted in December 1995. The regime had offered auto manufacturers reduced duties on imports of assembled cars and auto parts and other benefits if they exported sufficient quantities of parts and vehicles and promised to meet local content targets in their Brazilian plants. The Brazilian Government committed to eliminate the trade and investment distorting measures in its auto regime and not to extend the measures to its Mercosur partners when their auto regimes are unified in 2000. Mercosur is currently engaged in negotiations to unify its regimes, and the U.S. Government is closely following these talks.

Fiber Optic Cable: Due to concerns related to the certification of fiber optic cable, the United States persuaded the Government of Brazil to review fiber optic products solely on their merits. As a result, U.S. fiber optic cable was certified for sale in Brazil.

Intellectual Property Rights (IPR): In 1997 Brazil enacted laws providing protection of computer software, copyrights, patents and trademarks. While we have identified certain problems with some of this legislation, including a local working requirement and extensive exceptions to a prohibition on parallel imports in the patent law, overall the passage of these laws has brought the Brazilian IPR regime largely into line with international standards. The general thrust of intellectual property policy in Brazil has been to place greater emphasis on this subject as a critical element in enhancing Brazil's environment for investment and technological advancement. Nevertheless, the U.S. industry has voiced concerns with the high levels of piracy and counterfeiting in Brazil and the lack of effective enforcement of the copyright and trademark legislation. Problems have been particularly acute with respect to sound recordings and video cassettes. We also look to the Government of Brazil to ensure that its Patent Office (INPI) is given the resources and support necessary to fulfill its mandate. INPI has begun to issue pipeline patents for several high priority U.S. pharmaceutical products, and we have encouraged Brazil to focus on further improving its management of patent processing. The U.S. Government continues to work with Brazil on these matters.

Argentina

In 1998, the United States continued to run a trade surplus with Argentina of $3.8 billion. U.S. exports grew to an estimated $6.0 billion during 1998 from $5.8 billion in 1997. During the January 1999 State Visit of President Menem to the United States, President Clinton, Ambassador Barshefsky and other cabinet members pressed our bilateral and regional agenda and deepened our dialogue with Argentina on economic issues. An important factor in our trade relations with Argentina is the potential impact that the global financial crisis and Brazil's devaluation might have on its economy, especially given that Argentina trades more with Brazil than with any other country.

As in the case of Brazil, we encourage Argentina to continue its course of economic reform and trade liberalization. In that regard, we have expressed the view that Argentina should not increase customs duties. In addition, we have received assurances from the Argentine Government that it will not use a recent modification of the customs code in order to apply import duties on services, intellectual property and electronic transmissions.

Textiles, Apparel, and Footwear: In November

1997 a WTO dispute settlement panel ruled in favor of a U.S. challenge to duties and taxes assessed by Argentina that hinder market access for U.S. products. This decision was later upheld by the WTO Appellate Body. The panel found that Argentina's specific duties on textiles and apparel were excessive and violated Article II of the GATT. The panel also ruled that Argentina's three percent statistical tax on almost all imports is an impermissible charge in violation of GATT Article VIII. USTR will work in 1999 to ensure full implementation by Argentina of the WTO panel finding.

The panel determination did not specifically address footwear, given that the Government of Argentina had recast the specific duties on footwear as a safeguard measure immediately prior to the formulation of the WTO panel. The panel determined it could not provide relief with respect to measures that were no longer in effect. The U.S. Government believed that this footwear safeguard raised serious questions about Argentina's compliance with its WTO obligations, leading us to assert third party rights in the EC panel on this matter. Despite the questions raised on the WTO-consistency of Argentina's footwear safeguard, Argentina recently modified the measure in a manner that raises even greater concerns. Specifically, in November 1998 Argentina established a stringent tariff rate quota (TRQ) that will be imposed on footwear imports in addition to the safeguard duties already in effect; moreover, Argentina has delayed the time period for liberalizing the safeguard measure. The United States is troubled by this non-liberalizing modification of the safeguard measure, particularly in light of the requirements of Article 7.4 of the WTO Agreement on Safeguards, which clearly states that safeguard measures shall be progressively liberalized at regular intervals during the period of application. We have highlighted our concerns in our written submission to the panel reviewing the European complaint, and we are closely examining additional avenues to address this matter.

Intellectual Property Rights (IPR): Argentina's intellectual property regime does not yet meet TRIPS (WTO Agreement on Trade-Related Aspects of Intellectual Property Rights) standards and fails to fulfill long-standing commitments to the United States. Grave concerns regarding Argentina's IPR regime, particularly as regards pharmaceutical patent protection, led USTR to maintain Argentina on the Special 301 "Priority Watch List" in April 1998. In 1997 the Administration had withdrawn 50 percent of Argentina's benefits under the Generalized System of Preferences (GSP) over this same issue, and these benefits will not be restored unless our concerns are addressed adequately.

In some areas we have seen a recent deterioration of intellectual property protection, despite U.S. Government efforts, including in bilateral IPR talks in April 1998 and January 1999. In August 1998 the Argentine Government eliminated the ten-year exclusivity period for confidential test data for agrochemicals, which enjoy patent protection under Argentine law. This appears to conflict with the standstill provision in TRIPS. Also in 1998, the Government of Argentina failed to provide Exclusive Marketing Rights (EMR) to a U.S. company for a qualifying pharmaceutical product. This inaction by the Argentine Government raises doubts about such rights for other U.S. firms with products in line for EMR. Given that Argentina availed itself of the TRIPS transition period and delayed implementation of patent protection for pharmaceutical products, the GOA must provide EMR to innovative products that meet several conditions set out in the TRIPS Agreement. The U.S. Government is considering its policy options in both of these cases, including the possible pursuit of litigation at the WTO.

Argentina's copyright laws are currently under review by Executive Branch, and the U.S. Government is maintaining a dialogue with

Argentina on this review.

Pork: In October 1998, the Government of Argentina agreed to initiate the importation of fresh and processed pork meat from the United States. This provides a new market opportunity for U.S. pork producers at a critical time. The U.S. and the Argentine Governments are currently finalizing the import certificate that will allow these exports to commence, and we expect the text of this certificate to be finalized in the near future.

Paraguay

With a population of just over five million, Paraguay is one of the smaller U.S. markets in Latin America. To illustrate, in 1998 the United States exported a mere $780 million to Paraguay. However, Paraguay is a major exporter of and transshipment point for pirated products in the region.

Intellectual Property Rights (IPR): In January 1998, the USTR identified Paraguay as a “Priority Foreign Country” (PFC) under the “Special 301" provisions of the Trade Act. In identifying Paraguay as a PFC, the USTR noted deficiencies in Paraguay’s acts, policies, and practices regarding intellectual property, including a lack of effective action to enforce IPR. As required under the Trade Act, the USTR initiated an investigation of these acts, policies and practices in February 1998. In August 1998, the USTR extended the investigation until November in order to continue negotiations with the newly-elected Paraguayan Administration.

During these negotiations, the Government of Paraguay indicated that it had undertaken a number of actions to improve IPR protection, such as passing new copyright and trademark laws and undertaking efforts to improve enforcement. In November 1998, USTR concluded its investigation of the policies and practices of the Government of Paraguay concerning the protection and enforcement of IPR. The USTR determined that Paraguay’s acts, policies and practices regarding intellectual property rights are unreasonable and burden or restrict U.S. commerce; however, the USTR also decided not to take further action at this time, in light of commitments made by the Government of Paraguay in a bilateral Memorandum of Understanding (MOU), signed on November 17, 1998. The Government of Paraguay committed to take a number of near-term and longer-term actions to address the practices that were the subject of the investigation, including implementing institutional reforms to strengthen enforcement and taking immediate action against known centers of piracy and counterfeiting. The U.S. Government is currently monitoring Paraguay’s implementation of the MOU and will continue to do so in 1999, particularly as the “Special Enforcement Period” closes in March 1999.

Chile

During the State Visit of President Clinton to Chile in April 1998, the U.S. and Chilean Governments established the Joint Commission on Trade and Investment (JCTI). USTR Barshefsky and Chilean Foreign Minister Insulza signed the terms of reference for the JCTI in May 1998 and it met for the first time in Washington in October 1998. Topics discussed included WTO issues, the FTAA, APEC, GSP, intellectual property, liquor taxation, telecommunications and agricultural issues. The Joint Commission offers the United States and Chile a useful mechanism for addressing the full range of bilateral and multilateral issues and for consulting on how best to achieve progress in the FTAA negotiations.

The Administration remains committed to pursuing a comprehensive free trade agreement (FTA) with Chile, a recognized leader of economic reform and trade liberalization in Latin America, with growth averaging eight percent for a decade. While the economy slowed in 1998 due to the global financial situation, Chile’s GDP nonetheless grew by approximately four percent that year. As a resource-based economy, Chile has been seriously affected by the economic slowdown in many of its foreign markets, especially in Asia. Nevertheless, it has responded effectively to the global turbulence. It maintains the highest domestic savings and investment rates of any country in Latin America and unilaterally reduced its flat tariff by one percentage point to ten percent on January 1, 1999. Chile plans to reduce its tariff rate by one percentage point a year until reaching six percent in 2003. Chile is indicative of the potential of our trade ties with Latin America; U.S. exports to Chile have grown steadily in recent years, and in 1998, the Chilean economy absorbed more U.S. exports than either Argentina or Brazil, importing $4 billion worth of U.S. goods.

Chile has aggressively pursued free trade agreements and tariff-reducing agreements with its trading partners in the Americas and beyond, leaving the United States at a growing disadvantage in the Chilean market. Those countries with which Chile maintains special trade arrangements, which include most of our hemispheric trading partners, are exempt from Chilean tariffs or enjoy reduced rates.

Distilled Spirits: For several years, Chile has maintained a taxation system that discriminates against imported distilled spirits. In December 1997, Chile changed its law to phase in a system that is less obviously discriminatory, but that continues to burden U.S. exports. In January 1998, the United States and the European Union (EU) participated in GATT Article XXII consultations with Chile on this issue, and a WTO panel was subsequently established at the request of the EU. We asserted third party interest in this panel and in October submitted our third party brief in Geneva. The United States continues to express its concerns to the Government of Chile regarding the consistency of the taxes with Article III:2 of the GATT.

Uruguay

The smallest economy of Mercosur with a population of just over three million, Uruguay nonetheless imported $589 billion from the United States in 1998. The visit of President Sanguinetti in July 1998 gave our governments the opportunity to deepen our dialogue on trade matters. Issues addressed included coordinating our efforts in multilateral fora such as the FTAA and WTO and the importance of Uruguay’s efforts to bring its intellectual property regime into line with TRIPS standards by January 1, 2000.

The Andean Community

The U.S. trade deficit with the Andean region declined from $7.2 billion in 1997 to $2.5 billion in 1998, in large part due to the decrease in the price of oil imported from the region. U.S. exports to the region were down 1.1 percent in 1998 from 1997, totaling $15.4 billion.

The Andean Community originated as the Andean Pact in 1969, with Bolivia, Colombia, Ecuador, Peru and Venezuela as its members. However, it was only in the 1990's that the Andean Pact’s commitment to form a customs union took on momentum, with reduction and elimination of most duties between the members and an increasingly common external tariff. In 1997 the Andean Community became operational. Among its features are strengthened institutions, such as a Council of Presidents and a Council of Foreign Ministers in addition to meetings of Trade Ministers, and creation of a General Secretariat of the Andean Community mandated to act as the group’s executive body.

The Andean Trade Preference Act (ATPA) of 1991 authorizes the President to provide reduced-duty or duty-free treatment to most imports from Bolivia, Colombia, Ecuador and Peru. It is intended to help the four beneficiary countries expand economic alternatives in their fight against drug production and trafficking. ATPA preferential trade benefits are similar to those granted to beneficiaries of the Caribbean Basin Economic Recovery Act. ATPA preferences are scheduled to end on December 4, 2001. In December 1997 USTR submitted a triennial report to Congress on the operation of the program which indicated that the ATPA has facilitated economic development and export diversification in the ATPA beneficiary countries

Bilateral Investment Treaties: In April 1998 Ambassador Barshefsky signed a Bilateral Investment Treaty (BIT) with the Bolivian Government. The BIT is currently pending ratification by the U.S. Senate. It will help make Bolivia more attractive to potential U.S. investors and will provide investors in both countries guarantees of access and fair treatment in the other's market. During 1998 the U.S. Government also initiated formal BIT negotiations with the Government of Peru and continued negotiations with the Government of Venezuela. A U.S.-Ecuador BIT went into effect in May 1997.

Intellectual Property Rights: In the area of intellectual property the Andean Community countries have developed common disciplines with legal effect throughout the Community. The various Andean Pact decisions, while generally an improvement from previous disciplines, fall short in a number of ways in meeting WTO TRIPS requirements. The U.S. Government has been encouraging the Andean countries to, at a minimum, meet all TRIPS requirements by the deadline of the year 2000, but preferably to do so sooner.

Ecuador is on the Special 301 Priority Watch List. In May 1998 the Government of Ecuador adopted new, comprehensive intellectual property legislation. The Government had undertaken full TRIPS obligations upon its WTO accession as well as bilateral IPR commitments. While the legislation went a long way toward fulfilling Ecuador's international IPR obligations, we are working with the Ecuadorean Government regarding our remaining concerns with the law. We are also concerned that discriminatory provisions of the Dealers' Act may continue to be applied against U.S. companies. In Colombia, one particularly onerous situation facing U.S. television programmers involves the Government's failure to license legitimate subscription television stations. We are continuing to monitor IPR enforcement efforts in the region, which in general have improved marginally but remain inadequate.

Auto Regime: During 1998 the U.S. Government persuaded the Andean Governments to defer a planned extension of their automotive trade-related investment measures which would have violated their international obligations.

Trade and Investment Council Meetings: In October 1998 Ambassador Barshefsky and representatives of the Andean Governments signed an agreement establishing a U.S.-Andean Trade and Investment Council (TIC). The creation of this new partnership with the Andean Community members reflects the increasing importance the Andean Community has attained as a regional decision-making body and reflects the U.S. Government's interest in expanding our trade relationships in the region. The TIC will address key issues, such as the FTAA negotiations, protection of intellectual property rights, trade issues under the Andean Trade Preference Act, and matters of mutual interest in the WTO. During 1998 the U.S. Government also held bilateral TIC meetings with Colombia and Peru. We find these fora to be very helpful in strengthening our bilateral relations, and we look forward to holding further bilateral TIC meetings with our Andean trading partners.

Central America

The United States remains Central America's principal trading partner. Despite the devastating impact of Hurricane Mitch in October 1998, trade liberalization in Central America has continued, along with further regional integration in the Central American Common Market (CACM). CACM consists of Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua. Panama, which has observer status, and Belize participate in CACM summits but not in regional trade integration efforts. The CACM has created an internal market of over 31 million people with a combined GDP of over $44 billion. According to the World Bank, CACM's average per capita GDP of $1,375 covers a wide range from relatively wealthy Costa Rica (at $2,640) to still-struggling Nicaragua (at only $380). Even wealthier (at $3,080 per capita) is Panama, whose service-based economy contrasts sharply with the agriculture/textile based economies of CACM. Beyond CACM, additional efforts at trade integration in the region include agreements such as the Mexico-Nicaragua Free Trade Agreement, efforts to negotiate the Northern Triangle-Mexico Free Trade Agreement among Honduras, Guatemala, El Salvador and Mexico, and the proposed Panama-CACM Free Trade Agreement.

In March 1999, President Clinton joined leaders from Belize, Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua at the Antigua, Guatemala Summit. At the meeting, the leaders reaffirmed their desire to address issues of mutual concern with the U.S. both bilaterally and at the regional level through the Trade and Investment Council mechanism. These meetings provide fora for discussion of common trade and investment interests and will, in the future, permit consideration of electronic commerce. The President assured his counterparts from Central America and the Dominican Republic of his commitment to seek enhancements to the Caribbean Basin Initiative for the region. In the wake of the catastrophic economic consequences of Hurricanes Mitch and Georges, the regions' leaders are urgently seeking ways to promote job creation.

Intellectual Property Rights (IPR): Among the ongoing problems in the region is inadequate protection of intellectual property rights. The USTR is employing a regional strategy to promote more effective IPR protection. This has resulted in the signing of the Nicaragua-U.S. Intellectual Property Rights Agreement, improvement in IPR protection in Panama, and the ongoing negotiation of an IPR Agreement with Honduras. In the interim, the government of Honduras has recommitted itself in writing to implement fully its TRIPs obligations by January 1, 2000. Honduras also took effective action against television broadcasters who had been pirating copyrighted programming. In February 1998 Guatemala ratified the Paris Convention and later passed new copyright protection legislation. However, the Guatemalan government has yet to criminalize copyright offenses. USTR will continue to monitor closely IPR protection throughout Central America and to take appropriate action to ensure adequate and effective protection for intellectual property rights.

The Caribbean

Countries in the Caribbean region include members of the Caribbean Community and Common Market (CARICOM), and the Dominican Republic. Current members of CARICOM are: Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Suriname, and Trinidad and Tobago.

At the CARICOM-U.S. Trade and Investment Council meeting in September, 1997, trade officials agreed to create a mechanism to allow for rapid consultation ("quick consult") on trade related issues. They also discussed a framework for an agreement on electronic commerce and means to reduce existing trade barriers. The "quick consult" mechanism was used in October, 1998, when representatives of the CARICOM countries met in Washington with Ambassador Barshefsky to discuss the U.S. position on the EU banana case in the WTO. Follow-up discussions have been held with the objective of identifying WTO- consistent solutions that would be mutually beneficial to the U.S. and banana-exporting countries in the Caribbean and Latin America.

Participation in the Free Trade Area of the Americas process as well as the increased openness of most Caribbean economies and the growth of foreign direct investment should lead to future accelerated growth. These countries will be challenged to make the structural reforms needed to take maximum advantage of the benefits to be derived from a hemisphere-wide free trade zone. However, the active role that they have taken in the FTAA (e.g., Barbados' role as Chair of the Joint Public-Private Sector Committee on Electronic Commerce Exports) is indicative of their determination to increase their competitiveness in the 21st Century's economy.

The Caribbean Community and Common Market (CARICOM)

In 1997, CARICOM, a customs union rather than a common market, voted to grant membership to Haiti, the poorest country in the hemisphere. How this will affect progress toward economic integration and a common external tariff (CET) remains to be seen. A fully implemented common market would significantly enhance the market potential of countries in CARICOM. However, progress toward establishment of the CET has been limited.

Other Caribbean Countries

Several countries in the region are not currently members of any of the subregional trade blocs discussed above. The Dominican Republic, the largest beneficiary of the Caribbean Basin Initiative program, does not belong to any regional trade association, but has increased cooperation with both Central America and CARICOM. There has been some discussion of a CARICOM-Dominican Republic trade agreement. Cuba is not a member of any regional trade agreement, although it is a member of the Association of Caribbean States, an agreement on political and economic cooperation. Cuba has initiated a dialogue with CARICOM for possible membership, but to date there have been no negotiations.

The Caribbean Basin Economic Recovery Act

The Caribbean Basin Economic Recovery Act (CBERA) was created by the Congress in 1984 to promote the economic revitalization of the Caribbean Basin. Its principal component is tariff preferences, including zero duties on most products imported by the United States from the Caribbean and Central America. The CBERA program, originally set to expire in 1995, was made permanent in 1990, with reduced tariffs provided for several leather goods and for most products assembled in CBI countries from 100 percent U.S. components. The program was enhanced in September 1991, with new or expanded duty-free coverage provided to 94 products. On October 1, 1996 the President's Report on the Operation of the Caribbean Basin Economic Recovery Act (CBERA) was submitted to the Congress. The report is available on the USTR homepage at www.ustr.gov.

Caribbean Basin Trade Enhancement: The Administration's proposal for enhanced trade benefits for Caribbean and Central American (Caribbean Basin) countries, the Caribbean Basin Trade Enhancement Act (CBTEA), was introduced in the 105th Congress. There were several other proposals to provide expanded tariff preferences to CBERA beneficiaries, particularly in the textiles and apparel sector. However, none of these legislative proposals passed Congress in 1998. A driving factor in these efforts at legislation included the interest in addressing the concerns of countries in the Caribbean Basin regarding the potential diversionary impact of the NAFTA on their exports to the United States, particularly exports in the textile and apparel sectors, in light of Mexico's negotiated preferences. The Administration continues to support Congressional efforts to grant enhanced trade preferences to CBI beneficiary countries and will work with the 106th Congress to obtain passage of CBI enhancement.

Africa

In February 1998, Ambassador Charlene Barshefsky created the Office of African Affairs, signaling increased engagement with sub-Sahara Africa. Prospects in this region of over 600 million people are promising given the recent growth rates in many of the countries. Trade opportunities for the United States should continue to increase as the African countries plan major capital investments in telecommunications, civil aviation, and information technology, all areas in which the United States is competitive. Regional economic integration can serve as a catalyst for liberalization and economic growth in sub-Sahara Africa, and owing to economies of scale, can help U.S. exporters find larger markets for goods and services.

Republic of South Africa

With the most diverse economy in the region, South Africa is the United States' second largest trading partner after Nigeria. In 1998, two-way trade amounted to $xxx billion.

Intellectual Property Rights

South Africa amended its Medicines Act in December 1997. The new law appears to empower the Minister of Health to abrogate patent rights for pharmaceuticals. It also would permit parallel imports. Implementation of the law has been suspended pending the resolution of a constitutional challenge in the South African courts. Undisclosed data also is not adequately protected under South African Law. The need to provide such protection quickly is demonstrated by the approval in South Africa of a generic copy of a medicine which still has undisclosed data protected from competitors' use in many countries. South Africa should also strengthen enforcement of intellectual property laws. U.S. industry estimates that losses to copyright piracy increased by 26% between 1996 and 1997. In June 1998, the United States held in abeyance implementation of four South African requests for additional GSP preferences pending progress on IPR protection. During the coming year, we look to the Government of South Africa to enact TRIPs-consistent legislation protecting undisclosed information, to make clear in regulations or legislation that the powers granted in the Medicines Act are consistent with its international obligations and to clarify what actions may be taken pursuant to that Act and under what circumstances. The United States has raised, and continues, to raise these issues as priority concerns.

Mozambique

A Bilateral Investment Treaty (BIT) was signed on December 1 with Mozambique. The treaty must be ratified by the U.S. Senate and the Mozambican congress. BITs provide fair treatment for both countries' investors. They also guarantee the free transfer of capital, profits and royalties, freedom from performance requirements that distort trade and investment flows, access to international arbitration, and internationally recognized standards for expropriation and compensation. In addition, the treaty obligations ensure maximum transparency in investment.

Four other sub-Saharan African countries have BITs in place with the United States: Cameroon, the Congo, the Democratic Republic of the Congo, and Senegal.

Trade and Investment Framework Agreements

During 1998, negotiations began on a Trade and Investment Framework Agreement (TIFA) with the government of South Africa and Ghana, they are expected to be signed in 1999. TIFAs establish a mechanism through addressing trade and investment issues and identifying and eliminating or reducing barriers to trade and investment.

Regional TIFAs

Negotiation of a TIFA the West African Economic and Monetary Union (WAEMU) began in 1998. WAEMU includes the countries of Benin, Burkina Faso, Cote d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal , and Togo.

Regional TIFA's have been effectively used in other parts of the world as tools to institutionalize dialogue with regional leaders on trade and investment liberalization, regulatory and judicial reforms, intellectual property rights protection, and other measures to enhance trade. TIFA's establish Councils on Trade and Investment, chaired by the United States Trade Representative and the Economic and Trade Ministers of the respective countries

GSP Cumulation

The changes to the GSP program announced on July 1, particularly focused on encouraging Sub-Saharan African countries to accelerate their economic integration and work collectively to expand their exports. African countries which are members of any one of the three regional associations will be permitted to accumulate their value-added contributions (on GSP imports) making it easier for these countries to meet the 35 percent value-added requirement of the GSP rule of origin. Specifically, these countries will be allowed to cumulate the direct costs of growth, production, manufacture and assembly of a product with other qualifying members of their association. GSP cumulation also supports regional integration efforts. Regional economic integration will expand market size and make member states more attractive to private investors, both local and foreign.

The cumulation benefit became immediately available to all members of the West African Economic and Monetary Union (Burkina Faso, Benin, Côte d'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, and Togo), in recognition of the advanced stage of economic integration already achieved by these countries. Two other regional organizations, the Southern African Development Community (SADC) and the Tripartite Commission of East African Cooperation (EAC) also have been designated as qualifying for cumulation. Four members of the SADC presently qualify for this benefit since they have ratified the SADC Trade Protocol. These countries are: Botswana, Mauritius, Zimbabwe, and Tanzania. The Protocol aims to create a free trade area among its fourteen members. Other members of SADC will be considered for this new benefit upon ratification of the protocol. These countries are: Angola, Democratic Republic of Congo, Lesotho, Malawi, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Zambia, and Zimbabwe.

EAC members are preparing to sign an agreement that will formalize their efforts at trade integration. Once the agreement is signed and ratified, the EAC members, Kenya, Tanzania and Uganda, will be eligible for GSP cumulation benefits.

Despite the increase in African GSP utilization in 1997, African countries still accounted for only 6.9 percent of total U.S. GSP use. Moreover, utilization remained concentrated among a small number of African beneficiary countries. Four countries, Angola, South Africa, Zimbabwe, and Malawi, accounted for more than 87 percent of GSP benefits utilized by sub-Saharan Africa. Eritrea and Gabon have applied for eligibility under the program.

The Administration looks forward to further expanding the trade opportunities for reforming African countries through passage of the African

Growth and Opportunity Act in the 106th Congress. Among other provisions, the bill will expand for reforming African countries, the list of products given duty-free and preferential treatment under the GSP program.

WTO: Enhanced Engagement

Technical Assistance

A series of regional and national workshops structured to help African countries better understand the WTO and the potential benefits that will result from additional commitments began in 1998 and will continue through 1999. The workshops will help to establish a core of WTO expertise in Africa.